

NATIONAL 7(a) LENDER GUIDE

U.S. Small Business Administration

Version Date:

5/17/04

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Introduction

Welcome to the 7(a) Loan Program Guide. The purpose of this Guide is to provide an overview of the 7(a) Loan Program to 7(a) Lenders. It is intended to provide some degree of depth about aspects of the program of most interest to Lenders. **However, it is not meant to replace or supersede SBA statutes, regulations, standard operating procedures (SOPs), and official Agency notices, or to establish new policies or procedures. To the extent there is a conflict with this Guide, SBA statutes, regulations, SOPs, and official notices will control.** Lenders have an obligation to maintain familiarity and comply with all SBA policies and procedures that govern the program, as they are revised from time to time.

To help the user of this Guide locate the actual in-depth policy or procedure outlined in the Guide, the appropriate section of the SOP or other source document is referenced throughout the Guide. The user should look for the notation that says “(SOP ____, Sub ____, Ch ____, ¶ ____, Pages ____)” which will give the Subpart, Chapter, and Paragraph within the SOP, followed by the appropriate page numbers.

To easily access an SOP chapter, regulation, notice, or SBA form electronically, SBA has designed a webpage for lenders available at www.sba.gov/banking.

CHAPTER 1 - LOAN PROCESSING

When a lender is approached by a small business to extend credit for the business's financial needs, the lender may choose to approve the request, decline the request, or approve the request contingent on receiving an SBA guaranty. A typical reason for a lender to approve a loan only with SBA's guaranty is that the loan term the small business needs to finance its operations and to repay the loan in a timely manner exceeds the lender's own policies. For example, the small business may need a five-year working capital loan but the lender's internal policies do not permit a working capital loan beyond three years. Another typical reason is that the business is a start-up where an analysis of repayment is based solely on projections.

When a lender accepts SBA's guaranty on a loan, the lender also accepts certain responsibilities in order to maintain the guaranty. These responsibilities include a determination that the borrower, the use of the loan proceeds, and the loan structure meet SBA's requirements. In addition, all the lender's actions when approving, closing, disbursing, and servicing the loan (including liquidation activity) must meet prudent lending standards and comply with applicable SBA policies and procedures. A lender risks an alteration of SBA's guaranty (including full denial of liability) if these requirements are not met.

7(A) Loan Submission Processes

The 7(a) Loan Program has several different processes by which a lender may obtain an SBA guaranty for its qualified borrowers. Depending on the process, the maximum guaranty percentage, the maximum loan amount, and the turn-around time vary. The following is a chart of the different methods available to a 7(a) Lender to obtain an SBA guaranty for its small business borrower (Chart No. 1).

METHODS LENDERS USE TO OBTAIN AN SBA GUARANTY - Chart #1

Process	Standard 7(a) Guaranty	Certified Lenders Program (CLP)	Preferred Lenders Program (PLP)	LowDoc	SBAExpress
Attributes					
Submission to SBA and SBA's level of review	Lender submits standard SBA application including all required exhibits to SBA for its review. SBA fully re-analyzes Lender's analysis for eligibility and credit.	Lender submits standard SBA application including all required exhibits to SBA for its review. SBA reviews Lender's analysis.	Lender submits an eligibility checklist for SBA's review. Credit decision delegated to Lender. Standard application is completed by borrower and Lender but not submitted.	Lender submits a two-page summary of credit and eligibility for SBA's review.	Lender submits the same eligibility checklist as PLP for SBA's review EXCEPT for those Lenders with delegated eligibility-determination authority who are not required to submit the checklist.
Lender requirements	Lender completes and submits in-depth analysis of repayment ability, collateral, management, and credit history. Specific type of financial statement analysis required by SBA. SBA determines if the borrower meets SBA's eligibility requirements. SBA prepares loan authorization.	Same as for Standard 7(a) PLUS Lender provides draft loan authorization using SBA-approved boilerplate.	Lender completes but does not submit in-depth credit analysis using SBA forms. Lender initially determines eligibility prior to completing checklist. Lender prepares authorization using SBA-approved authorization boilerplate but does not submit to SBA for its review.	Lender completes and submits summarized credit and eligibility analysis. Lender initially determines eligibility prior to completing forms. SBA prepares loan authorization.	Lender completes but does not submit credit and eligibility analysis using its own procedures. Lender initially determines eligibility prior to completing checklist. Lender is not required to use SBA authorization boilerplate.
Required documentation prepared by Lender	Application includes SBA Form 4 with all required attachments and SBA Form 4-I with all required attachments and analysis.	Same as Standard 7(a) PLUS draft loan authorization using SBA-approved boilerplate.	Same as Standard 7(a) PLUS eligibility checklist PLUS loan authorization (not reviewed by SBA) using SBA-approved boilerplate.	Lender uses own application forms. Completes 2-page submission to SBA.	Lender uses own forms. Lender uses own loan authorization. Lender completes eligibility checklist in some cases.
SBA's loan approval role	SBA determines eligibility and credit risk. SBA prepares and finalizes the loan authorization.	SBA determines eligibility and credit risk. SBA finalizes the authorization.	SBA makes eligibility determination based on completed checklist submitted by Lender.	SBA determines eligibility and credit risk. SBA prepares and finalizes the loan authorization.	Same as PLP
Size Standard	Regular size standard	Regular size standard	Regular size standard	Special size standard	Regular size standard
Target Proc. time	13 business days	3 business days	1 day	1.5 days	1 Day
Maximum loan amounts	General rule is gross loan amount limited to \$2,000,000 SBA guaranty amount limited To \$1,500,000 . (Chart 2 for exceptions.)	Same as Standard 7(a)	Same as Standard 7(a)	Limited to \$150,000 (gross)	Limited To \$2,000,000 (gross)
Percent of Guaranty	85% for loans of \$150,000 or less. 75% for loans over \$150,000 .	Same as Standard 7(a)	Same as Standard 7(a)	Same As Standard 7(a)	50%
Use of Proceeds	Refer to Chart 2 which describes the various programs and their limitations.	Same as Standard 7(a)	No refinancing of Same Institution Debt (SID) permitted.	SID refinancing limited to 25% of loan.	No refinancing of SID permitted.
Maturity	Depends on use of proceeds and which loan program used. Maximum of 25 years reserved for fixed assets including real estate.	Same as Standard 7(a)	Same as Standard 7(a)	Same as Standard 7(a)	Maximum of 7 years.
Interest Rates	Prime + 2.25% for loans with maturities under 7 years . Prime + 2.75% for 7 years or more . Special exception for loan amounts of \$50,000 or less : rates can be higher.	Same as Standard 7(a)	Same as Standard 7(a)	Same as Standard 7(a)	Loans \$50,000 or less: Prime + 6.5%. Over \$50,000: Prime +4.5%
Guaranty Fees (Multiply percentage times guaranteed amount, not gross amount.)	Maturity of 12 months or less = 0.25% On maturities over 12 Months Gross loan: \$150,000 or less = 1% Gross loan \$150,001 - \$700,000 = 2.5% ;Over \$700,000 = 3.5% ; Additional .25% of the guaranteed portion which exceeds \$1,000,000.	Same as standard 7(a)	Same as Standard 7(a)	Same as Standard 7(a)	Same as Standard 7(a)

Maximum Loan Maturities

The specific maturity of a loan is determined by:

- use of proceeds
- ability to repay
- useful life of the assets being financed

The maximum maturities permitted by SBA are the following:

For **long term working capital**, 10 years;

For **fixed assets**, the economic life of those assets up to 25 years. (The 25-year maximum maturity normally applies only to the acquisition of land and buildings or the refinancing of debt incurred in the acquisition or construction of land and buildings. If the 7(a) loan covers the construction period, the 25-year maximum would be **in addition to** the time needed to complete construction.) Generally equipment loans are limited to 10 years or less.

When the loan proceeds are to be used for **varied purposes**, the maximum maturity and resulting amortization is a **weighted average of the uses of the proceeds**.

For loans to franchises, the term of the loan is generally no longer than the term of the franchise agreement.

A summary of the various loan programs is found in Chart No. 2 and includes the different uses of proceeds, maturities, collateral, and qualifications.

SBA LOAN PROGRAMS REFERENCE GUIDE – Chart #2

Program	Use of Proceeds	Special Features	Maturity	Collateral	Who Qualifies
Basic 7(a) Loan (See "C" below.)	Acquisition or construction of buildings (including land); machinery and equipment; furniture and fixtures; leasehold improvements; short or long-term working capital; refinancing.	The most flexible. Adaptable to a variety of loan structures for a variety of loan purposes. There are general (government) restrictions on what the proceeds can be used for and the types of businesses that can receive financial assistance from SBA.	Working Capital up to 10 years. Fixed Assets including Real Estate up to 25 years. Maturities combine 1) use of proceeds and 2) business's ability to repay in a timely manner.	The goal is to take available collateral (valued at the liquidation value) equal the loan amount. Collateral may include all assets financed with loan proceeds; other business assets; and personal assets of principals. If all available collateral does not fully secure the loan, that is acceptable BUT it is not acceptable if the loan is not secured by all available collateral.	Must be eligible incl. being a for-profit business that meets certain size standards; cannot obtain loan proceeds for an ineligible purpose; owners must be of good character. Must be creditworthy including reasonably demonstrate that the loan (with all other obligations) can be repaid from the operations of the business in a timely manner.
International Trade Loan Program (See "B" below.)	Finances fixed assets including improvements that will be located in the U.S. and used to produce goods/services to be exported. No refinancing allowed	When made in conjunction with a working capital loan, the two loans together can have a SBA guaranteed share up to \$1,250,000	Based on the assets being financed. Generally between 10 and 25 years	Must be secured by a first lien on the assets acquired with the loan proceeds.	Same as Basic 7(a) PLUS the applicant must have been in operations at least 12 months at the time of application..
Export Working Capital Program (EWCP) (See "B" below.)	Finances the short term working capital needs of a exporting business on either a revolving or non-revolving basis	Prequalification by SBA available prior to small business applying to Lender. SBA provides a 90% repayment guarantee up to \$1 million. Only program with a provision for a Standby Letter of Credit to offset risk.	Generally 12 months or less, with annual reissuances for a maximum of 3 years.	First on the assets being financed.	Same as Basic 7(a) PLUS the applicant must have a prior (12 month minimum) history of demonstrated export expertise
Seasonal CAPLines (See "A" below.)	Finance the seasonal working capital needs. New businesses ineligible.	Mandated zero balance at season's end prior to future season draws.	Maximum of 5 years	First on the assets being financed.	Same as Basic 7(a) PLUS business in operation for at least one year with a definite seasonal pattern to sales/expenses
Contract CAPLines (See "A" below.)	Finance the direct costs needed to perform on an assignable contract	Can provide loan funds prior to start of work.	Maximum of 5 years	Assignment of the proceeds from the contract(s) being performed.	Same as Basic 7(a) PLUS business must have demonstrated, historical experience performing on same type contract.
Builders CAPLines (See "A" below.)	Finance the Contractors cost to build or renovate commercial or residential property to be resold to a third party upon completion	The only SBA program that allows a business to buy a building or home for the purpose of being resold.	Maximum of 5 years	First on the assets being financed.	Only available to businesses in the built and construction trades.
Small Asset Based CAPLines (See "A" below.)	Provides working capital based on eligible accounts receivable and inventory. Limit of \$200,000	Required review of a monthly borrowing base by lender to ensure that borrowing does not exceed qualified assets.	Maximum of 5 years	First on the assets being financed.	Same as Basic 7(a) PLUS designed for businesses who sell on credit and who have a need to obtain funds from existing receivables and inventory prior to receiving funds from customers
Standard Asset Based CAPLines (See "A" below.)	Provides working capital based on eligible accounts receivable and inventory.	Borrowing base review by Lender with each request for disbursement. No restriction on servicing fee charges by lender subject to full disclosure	Maximum of 5 years	First on the assets being financed	Same as Small Asset Based CAPLines.
Energy Loan Program (See "A" below.)	Provides financing to develop, build, install and/or service an energy savings device.	The only SBA loan program that permits loan proceeds to be used for Research & Development (up to 30%)	Same as Basic 7(a)	Same as Basic 7(a)	Same as Basic 7(a) PLUS business has to make, build, improve, install or service the energy savings device. (See pages 232-234 of SOP 50-10(4).) This program is not for the end user of the energy device or measure.
Employee Stock Ownership Plan (ESOP) Loans (See "A" below.)	Provides funds to ESOP to purchase or increase the ESOP's ownership in the business that employs its owners.	The loan is made to the trust, not the business. Other special requirements are on pages 242 to 249 of SOP 50-10(4).	Same as Basic 7(a)	Same as Basic 7(a) BUT the ESOP Trust is not required to guaranty.	A qualified Employee Trust organized under IRS or Department of Labor Requirements

A - Can be processed only under Standard 7(a).

B – Can be processed under Standard 7(a) or PLP.

C – Can be processed under all methods. (See Chart No. 1 for methods.)

Fees

GUARANTY FEES

(SOP 50-10(4), Sub B, Ch 1, ¶ 15, Pages 214 to 221-6)

Guaranty fees are paid to SBA to support the cost of the program resulting from SBA's honoring its guaranty when a 7(a) borrower fails.

One-Time Guaranty Fee (13 CFR 120.220)

The lender pays a one-time fee when the loan is approved. It is a flat fee based on the size of the loan, the amount guaranteed by SBA, and the term of the loan.

For loans with a maturity of 12 months or less, the guaranty fee is .25 of 1 percent of the guaranteed amount.

For loans with a maturity exceeding 12 months, the guaranty fee is as follows:

Gross Loan Size:	\$150,000 or less	= 1.0% of guaranteed amount
	Over \$150,000 to \$700,000	= 2.5% of guaranteed amount
	Over \$700,000 to \$2,000,000	= 3.5% of guaranteed amount*

*There is an additional up-front guarantee fee equal to 0.25 percent of the amount by which the guaranteed portion exceeds \$1,000,000.

Lenders can charge the fee to the Borrower AFTER the Lender pays it and AFTER the loan is closed and disbursed.

Combination Loan Financing

If the commercial lender has a senior credit position to the 7(a) loan, a one-time fee equal to **0.7 percent of the amount of the commercial loan** is to be paid to SBA.

This fee shall be paid by the SBA participating lender, and must be remitted when the up-front guarantee fee is paid. This fee may not be passed on to the borrower.

If the commercial loan is in a shared lien (sometimes known as pari passu) or subordinate lien position to the 7(a) guaranteed loan, this one time fee does NOT apply.

On-Going Guaranty Fee (13 CFR 120.220 (f))

The Lender pays SBA an annual servicing fee equal to 0.36% of the outstanding principal balance of the guaranteed portion of the loan. Unlike the flat fee, Lenders are not permitted to pass this fee onto the Borrower.

Subsidy Recoupment Fee Payable to SBA by Borrower (13 CFR 120.223)

For loans with a maturity of 15 years or more, a subsidy recoupment fee is assessed of the borrower when the borrower voluntarily prepays 25% or more of its loan in any one year during the first three years. The fee is 5% of the prepayment amount during the first year, 3% during the second year, and 1% during the third year.

OTHER FEES

Fees a Lender May Collect (13 CFR 120.221): (SOP 50-10, Sub B, Ch 1, ¶ 16, Page 222)

Packaging Fees: The Lender may charge an applicant reasonable fees that are customary for similar services provided by lenders in the geographic area where the loan is being made. SBA may review these fees at any time. The Lender must refund any such fee considered unreasonable by SBA.

Closing expenses: The Lender may collect from the applicant necessary out-of-pocket expenses such as the costs associated with surveys, title reports, appraisals, filing and recording fees, photocopy and delivery charges, and other direct charges related to the closing. The Lender or a Lender's associate may not charge the Borrower for legal services, unless they are hourly charges for requested services actually rendered.

Extraordinary servicing: Subject to prior written SBA approval, if all or part of a loan will have extraordinary servicing needs, the Lender may charge the applicant a servicing fee not to exceed 2 percent per year on the outstanding balance of the part requiring special servicing. Examples are 7(a) loans that cover the construction period which would include field inspections, monitoring of draw schedules, title reports, etc.; or asset based lending secured by accounts receivable and/or inventory that require frequent monitoring and inspections of that collateral.

Fees a Lender May Not Collect (13 CFR 120.222) (SOP 50-10, Sub B, Ch 1, ¶ 17, Pages 222 to 226)

Application fees: Processing fees, origination fees, application fees, points, brokerage fees, bonus points, add-on interest, commissions, referral or similar fees which the Lender might charge an applicant on a commercial loan are not permitted for a 7(a) loan.

Premiums: The Lender or its Associate may not share any premium received from the sale of a 7(a) loan in the secondary market with any other entity or individual not directly compensated by the lender.

Prepayment Fee: The Lender may not charge a fee for full or partial prepayment of a loan.

Fees for goods or Services such as Insurance: The Lender is prohibited from collecting fees for goods or services, including insurance, as a condition of obtaining an SBA guaranteed loan.

Interest Rates

Variable Rate Loans

The initial interest rate for a variable rate loan is based on the prime rate printed in the Wall Street Journal on the date SBA receives the loan application. This date is identified in the loan authorization.

The percentage above the prime rate must not exceed:

- 2.25%—If Loan is more than \$50,000 and matures in less than 7 years.
- 2.75%—If Loan is more than \$50,000 and matures in 7 years or more.
- 3.25%—If Loan is for \$25,001-\$50,000 and matures in less than 7 years.
- 3.75%—If Loan is for \$25,001-\$50,000 and matures in 7 years or more.
- 4.25%—If Loan is \$25,000 and under and matures in less than 7 years.
- 4.75%—If Loan is \$25,000 and under and matures in 7 years or more.

(Refer to Chart #1 for *SBAExpress* interest rates)

A Lender is prohibited from increasing the initial interest rate until the first day of the first fluctuation month occurring after initial disbursement.

There is no requirement that the loan payment amount change at the same frequency as interest rate changes. However, the Lender must adjust the payment amount **at least annually** to ensure that the principal amortizes over the remaining term of the loan.

Ceilings and Floors

A Lender may establish interest rate ceilings and floors, however,

1. Both the ceiling and floor must be stated in the Note, and
2. The difference between the stated rate in the Note and the floor must be equal to or greater than the difference between the stated rate in the note and the ceiling. For example: if the rate is 10% and the ceiling is 12%, then the floor must be 8% or lower.

Eligibility

Once a Lender has initially reviewed the application and determined that the Lender's policies do not permit it to approve this loan without SBA's guaranty, the Lender then must determine if the applicant is eligible to receive SBA financial assistance. There are five basic factors to consider when determining eligibility.

1. Size and affiliation
2. Type of Business
3. Use of Proceeds
4. Credit Elsewhere
5. Special Eligibility Factors:
 - Eligible Passive Company (EPC)
 - Change of Ownership
 - Foreign-Owned Businesses or Businesses Owned by Non-U.S. Citizens
 - Farms and Agricultural Businesses, and Medical Facilities
 - Litigation, Bankruptcy, Probation or Parole
 - Combination Financing (sometimes referred to as Piggyback Financing)

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SIZE AND AFFILIATION

(SOP 50-10(4), Sub A, Ch 3, Pages 71 to 80-1)

Size

SBA can only guaranty loans made to small businesses. To determine whether a business is small, SBA uses the North American Industry Classification System (NAICS). SBA has posted the Table of Small Business Size Standards from the NAICS manual on its website at www.sba.gov/size.

Under NAICS, the standard for an industry is based on **either the number of employees** (calculated by averaging the total number of employees for each pay period during the most recently completed 12 calendar months) **or** average **annual receipts** for the most recently completed 3 fiscal years. A synopsis of SBA's basic Size Standards follows.

<u>Industry</u>	<u>Size Range</u>
Retail and Service	\$1.5 to \$24.0 million
Construction	\$12.0 to \$28.5 million
Agriculture	\$0.75 to \$10.5 million
Wholesale	No more than 100 employees
Manufacturing	500 to 1,500 employees

A business that meets SBA's size standards at the time of application is eligible even if the loan proceeds will result in an increase beyond those standards.

Affiliation (SOP 50-10(4), Sub A, Ch 3, ¶ 3, Pages 71 to 75)

Size is determined based on the combined operations of an applicant and all its affiliates. (Concerns are affiliates of each other when one concern controls or has the power to control the other, or a third party or parties controls or has the power to control both.) Businesses that have common ownership, common management, or contractual relationships may be affiliates. When affiliation exists between companies, two separate size standard tests must be met. The applicant must not exceed the size standard for the industry in which:

1. The applicant and its affiliates are primarily engaged
2. The applicant alone is primarily engaged.

When two or more businesses are affiliated and they each conduct different business activities (for example manufacturer and wholesaler), the primary business activity must be determined.

Where the affiliates are engaged in several industries, the size standard is that of the primary industry of all the related concerns taken as a whole.

If the business or its affiliate already has an SBA guaranty loan outstanding, the dollar amount of any subsequent SBA loan request is added to the outstanding amount of all SBA loans to ensure that the combined loans do not exceed SBA maximums to one borrower (including affiliates).

Franchises (SOP 50-10(4), Sub 3, Ch 3 ¶ 3e, Page 75)

If the applicant is a franchisee, a special determination of whether the franchisee is affiliated with the franchisor needs to be made. If affiliation is determined, the franchisee is not eligible to apply by itself. Affiliation may arise through common ownership, common management or excessive restrictions imposed by the franchise agreement.

To streamline the determination of whether affiliation exists between selected franchisees and franchisors or licensees and licensors, SBA has established a Franchise Registry, www.franchiseregistry.com. This Registry lists those franchises that have paid to have their agreements reviewed **and** that SBA has determined have an agreement that does not create an affiliation between the franchisor and the franchisee. Participation in the Registry by any given franchise is voluntary. A fee is paid by the franchisor in anticipation of being listed so that when one of their existing or potential franchisee operations applies for SBA financing the determination of one of the more involved aspects of SBA eligibility can already be completed.

If a franchise is not listed on the Registry, an eligibility review must be performed. If the loan is processed by SBA, SBA is responsible for the review. If a loan is submitted under delegated authority, the lender is responsible for reviewing the franchise documents and making the eligibility determination. Appendix 1-A of this guide is a checklist for use in determining whether a franchise is eligible.

(Note: a determination that the franchise is eligible does not address all aspects of eligibility, but rather only the issue of whether the franchise relationship between the Borrower and its

franchisor creates an affiliation that would affect the Borrower's small business size status and, therefore, eligibility for SBA-guaranteed financing.) For franchises listed on the Registry, the Lender only needs to obtain a "Certification of No Change or Non-Material Change on Behalf of Registered Franchisor" signed by the franchisor. If the franchise is not listed, a written determination of eligibility opinion must be made.

Some of the criteria that SBA reviews are the following:

- Franchise Fee and other fees are not excessive.
- Franchisee has control of money & accounts – deposits and withdrawals. (Franchisor may prescribe accounting method and due dates for fee payment, but may not control accounts.)
- Franchisee manages daily operations (except in case of illness or disability).
- Franchisee controls, hires and fires employees. (Franchisor can require employee training.)
- Agreement specifies: 1) events of default; 2) what written notice of default will be provided; 3) events that may lead to termination; 4) events that cause automatic termination; and 5) time to cure provided for other defaults.
- Franchisee has the right to transfer its interest in the franchised business.
- Franchisor allows transfer to qualified transferee. (Qualifications must be specified in Agreement or otherwise set forth in writing.)
- Franchisor prior written consent will not be unreasonably withheld or delayed.
- Franchisor does not control sale price or appraisal method.
- Terms and conditions of leases and/or other franchise related documents do not lead to excessive Franchisor control.

TYPE OF BUSINESS

(SOP 50-10(4), Sub A, Ch 2, ¶ 8, Pages 28 to 44)

Most types of businesses **are eligible** for financial assistance from SBA. To be eligible a small business must be:

- Organized for profit.
- Open to the public on a non-discriminatory basis.
- Located in the United States or its possessions.

The following are **not eligible for SBA financial assistance**:

- Non-Profit Businesses
- Businesses Primarily Engaged in Lending
- Passive Holder of Real/Personal Property: Entities that exist to passively hold real or personal property principally to collect the rental income from such properties are not eligible for SBA financing.
- Life Insurance Companies: Life insurance agencies, however, may be eligible for SBA financial assistance provided they are considered independent contractors and have no affiliation with the companies they represent.

- **Businesses Located in a Foreign Country**
- **Businesses Selling Through a Pyramid Plan**
- **Businesses Engaged in Gambling:** Businesses deriving more than one-third of gross annual revenues from legal gambling activities are not eligible for SBA financing. Businesses generating 33% or less from legal gambling are eligible if the activity is licensed and supervised by the appropriate state authority.
- **Illegal Businesses:** Businesses that directly engage in illegal activities and businesses that knowingly sell, service, or distribute legal products specifically used in support of illegal activities.
- **Businesses Which Restrict Patronage:** Businesses that restrict membership or patronage for any reason other than capacity (e.g. based on ethnicity, religion, gender, etc.).
- **Government Owned Entities (Excluding Native American Tribes):** SBA financing to assist municipalities or other political sub-divisions is prohibited as financial assistance from other Federal agencies is available to such entities. While Native American tribes are considered government entities, tribally-owned small businesses may be eligible for SBA assistance. Such businesses must establish legal distinction from the tribe, and lenders should ensure that the tribe has the authority to establish the applicant and that appropriate provisions are made to ensure collectability of the debt (e.g., waiver of sovereign immunity).
- **Businesses Engaged in Promoting Religion:** Businesses principally engaged in teaching, instructing, counseling or indoctrinating religion or religious beliefs. Businesses that primarily offer tangible religious items, broadcast religious music, publish religious periodicals or develop religious software may be eligible despite the religious aspect of the enterprise. Also, while non-profit religious entities are ineligible for SBA assistance, their for-profit subsidiaries may be eligible.
- **Consumer or Marketing Co-operatives:** Producer co-operatives, however, may be eligible. Eligibility requires the co-operative to be engaged in a business activity and to be organized for the financial benefit of both the co-operative and the member businesses, all of which must be considered small.
- **Businesses Engaged in Loan Packaging:** Loan packagers deriving more than one-third of their gross revenue from packaging SBA loans are ineligible for SBA financial assistance.
- **Businesses Providing Prurient Sexual Material**
- **Businesses That Have Previously Defaulted on a Federally Assisted Financing Resulting in a Loss to the Government:** This includes businesses owned or controlled by an applicant or any of its Associates (“Associate” is defined in 13 CFR Section 120.10) which previously owned, operated, or controlled a business which defaulted on a Federal loan (or guaranteed a loan which defaulted) and caused the Federal government to sustain a loss in any of its programs (for purposes of this section, a compromise agreement shall also be considered a loss).
- **Businesses Primarily Engaged in Political or Lobbying Activities.** This includes businesses where 50% or more of the applicant’s revenues or time are related to such activities.

- Speculation: SBA financial assistance is prohibited if the applicant business is principally engaged in speculation in any kind of property (real, personal or intangible).

USE OF LOAN PROCEEDS

(SOP 50-10(4), Sub A, Ch 2, ¶ 10, Pages 51 to 60)

SBA 7(a) loans may be used for most business purposes that benefit the small business including: (SOP 50-10(4), Sub A, Ch 2, ¶ 10, Page 51)

- Acquisition, construction or renovation of buildings
- Purchase of equipment, fixtures or inventory
- Working capital
- Refinancing of existing debt
- Purchase of existing businesses

SBA loan proceeds **must not** be used for any of the following purposes: (SOP 50-10(4), Sub A, Ch 2, ¶ 11, Pages 52 & 53)

- Finance floorplan needs
- Purchase real estate where the participant has issued a forward commitment to the builder/developer
- Pay delinquent withholding taxes, sales tax or similar funds held in trust for a purpose other than use by the business
- Make payments to an Associate or principal of the business
- To acquire real estate that will be held primarily for investment purposes (exception is for Eligible Passive Companies discussed later).

Debt Refinancing Restrictions: (SOP 50-10(4), Sub A, Ch 2, ¶ 12, Pages 54 to 60)

To be eligible for refinancing by SBA, existing debt must not be on reasonable terms AND the refinancing must provide a substantial benefit to the small business. SBA has four basic rules pertaining to debt refinancing:

1. Refinancing cannot be used to provide an extension of credit for a purpose which is not otherwise eligible: The original purpose of the debt being refinanced had to have been eligible for SBA financing when originally made or the ineligibility has to have been eliminated prior to the approval of a refinancing.
2. Refinancing must provide the business with a substantial benefit: SBA measures the benefit by comparing the dollar amount of the monthly payment of a debt prior to being refinanced to the dollar amount of the monthly payment after refinancing. SBA requires at least a 20% reduction in the amount of the loan payment for any amortized debt with regularly scheduled principal and interest payments and a maturity over 12 months.

There are exceptions to the 20% test. SBA considers the following types of refinancing requests to be beneficial to the business even though the 20% test is not met:

- Debt structured with a maturity of 12 months or less requiring just interest only payments until maturity.
- A business related credit card debt that does not require a minimum payment to bring all interest current through the date paid plus reduces the principal that was owing at the time of billing by at least 5%. SBA will consider refinancing credit card debt if the applicant documents that the use of the credit card was business related. The application must include documentation to support that the debt was business related.
- Trade payables classified as short-term debts. Working capital proceeds can be used by an eligible small business to reduce or pay off that business's accounts payable and not be subject to either the substantial benefits or unreasonable terms test.
- Debt amortized with a balloon payment.

3. The debt being refinanced must be on unreasonable terms prior to refinancing. The principal test for how reasonable the terms of the existing debt are is whether the existing cash flow of the business is adequate to meet these obligations. If the payments are in excess of what an analysis of repayment and cash flow determines the business can reasonably pay, then the debt can be classified as being on unreasonable terms.
4. SBA prohibits loan proceeds from being used to pay a creditor who is in a position to sustain a loss. In such cases, refinancing would cause a shift to SBA of all or part of a potential loss from an existing debt.

On all debt refinancing, the following is required:

- Copies of all original and renewal notes.
- An explanation of what the original proceeds were used for and what collateral was given to secure the debt.
- Maturity tied to the original purpose of the loan.

Refinancing Participant's Own Non-SBA Debt: (SOP 50-10(4), Sub A, Ch 2, ¶ 12(c), Page 58)

For all debt refinancing, the lender must:

Certify in writing that subject debt is and has always been current for the entire period the loan has been outstanding up to 36 months, whichever is greater. Current means that a required payment has not remained unpaid for more than 29 days. (A loan that includes a payment unpaid for 30 days that subsequently was deferred is considered not current on that 30th day and is therefore not eligible for refinancing.)

Provide a transcript of the borrower's account with the application showing that the loan to be refinanced is current and has been current for at least the last 36 months.

Refinancing Non- Participant SBA Debt: (SOP 50-10(4), Sub A, Ch 2, ¶ 12(a) & (b), Pages 54 to 57)

A Lender can refinance existing SBA debt held by another lender ONLY if the Lender is able to demonstrate that the debt is eligible for refinancing AND the current lender is unwilling or unable to modify the terms to accommodate the borrower's current needs and repayment ability.

Refinancing Participant SBA Debt: (SOP 50-10(4), Sub A, Ch 2, ¶ 12(d), Page 59)

SBA will not consider a request to refinance a participant's SBA debt with one exception: If in order to assist the borrower, the loan needs to be reamortized AND the loan has been sold in the secondary market AND the purchaser (investor) will not permit a renegotiation of the terms, SBA may consider the request to refinance.

CREDIT ELSEWHERE TEST

(SOP 50-10(4), Sub A, Ch 2, ¶ 3 and 4, Pages 11 to 23)

SBA cannot provide financial assistance to small businesses that have the ability to obtain the financing without federal assistance. This means that funds must not be available on reasonable terms from any of these sources:

The lending institution: If a lending institution can provide the credit to the small business applicant on reasonable terms without SBA's guaranty, then the requested financing is not eligible for SBA consideration. In order to be eligible, the loan documentation must identify a reason why the loan request does not meet the lender's established policies or regulatory restrictions.

The internal resources of the applicant concern: SBA requires that borrowed funds be unobtainable through the disposal, at a fair price, of assets owned by the applicant business, if these assets are not needed by the business to conduct its operation or not reasonably necessary for healthy growth.

The external resources of the applicant concern: SBA also requires that borrowed funds must be unobtainable through the disposal, at a fair price, of assets owned by any of an applicant's affiliates, that are not needed by the affiliate for its operation or that are not reasonably necessary for the affiliate's healthy growth.

The personal resources of the owners of the applicant concern: SBA requires the use of personal resources from any 20% or more owner as an injection to reduce the SBA funded portion of the total financing package. When the total financing package:

1. Is \$250,000 or less, each 20% owner of the applicant must inject any personal liquid assets which are in excess of two times the total financing package or \$100,000, whichever is greater; or
2. Is between \$250,001 and \$500,000, each 20% owner of the applicant must inject any personal liquid assets which are in excess of one and one-half times the total financing package or \$500,000, whichever is greater; or

3. Exceeds \$500,000, each 20% owner of the applicant must inject any personal liquid assets which are in excess of one times the total financing package or \$750,000, whichever is greater.

Requirements of the rule are:

1. Only individuals (not businesses) who own 20% or more of the small business concern or the eligible passive company are subject to this rule. (Spouses and any dependent children with a combined ownership interest of 20% or more in the applicant or eligible passive company are subject to the rule.)
2. The exemption thresholds are based on the total financing package, not just the loan that SBA guarantees.
3. Only liquid assets are subject to the rule.

There are no additional exemptions. This means there are no exemptions for education, retirement funds not subject to withdrawal restrictions or other penalties, medical reserve fund, business contingency, or any other type of exemption that originates from a personal desire.

SPECIAL ELIGIBILITY FACTORS

(Various locations within SOP 50-10(4), Subpart A)

In addition to the standard eligibility issues of size, type of business, use of proceeds, and credit elsewhere, there are also some other special factors that impact eligibility.

Eligible Passive Concerns (EPC) (SOP 50-10(4), Sub A, Ch 2, ¶ 9, Pages 45 to 50)

As previously stated SBA is prohibited from providing financial assistance to businesses owned by developers or landlords. SBA allows one exception—a loan structure where the Borrower is a passive owner of the assets to be financed with the loan proceeds and leases the assets to an Operating Company (OC). The Borrower in these cases is an Eligible Passive Company (EPC). SBA has several special requirements that must be met when the loan has an EPC/OC structure:

- The OC must be an eligible small business, and the proposed use of the proceeds must be an eligible use as if the OC were obtaining the financing directly.
- The EPC and the OC each must be small under the appropriate size standards. When determining size, the EPC is not combined with the OC unless an affiliation exists. The fact that the EPC is leasing the project property to the OC does not in and of itself create an affiliation.
- There can be multiple OCs but only one EPC.

- All parties must be liable:
 - EPC as Borrower
 - OC as either a Guarantor or Co-Borrower
 - All 20% or more owners of both the EPC and OC must guarantee the loan in full.
- OC MUST be a Co-Borrower when:
 - Any assets purchased with loan proceeds will be directly owned by the OC and appear on the OC's balance sheet
 - Use of proceeds includes working capital
- There must be a written lease for 100% of the property financed with loan proceeds from the EPC to the OC and:
 - Lender must obtain a perfected assignment of rents paid under the lease between the EPC and the OC.
 - Term of the lease, with options to renew, must be equal to or exceed the term of the loan.
 - Lease payments must not exceed the amount necessary to cover the amortization of the SBA 7(a) loan plus any expenses related to maintaining the property as well as paying property taxes and insurance. Lease payments cannot include a profit margin to the EPC.

Change of Ownership (SOP 50-10(4), Sub B, Ch 3, Pages 193 to 199)

Loan proceeds may be used to accomplish a change in ownership of a small business where:

- The transaction will result in the Borrower acquiring/owning 100% of the business;
- The buyer(s) and seller(s) are involved in an arms-length transaction, and the price to be paid represents the fair market value of the business; and
- There is a reasonable need for the change in ownership, e.g., the change in ownership will promote the sound development of the small business, or will preserve the existence of the small business.

Acquisition of a Existing Business

Issues that the Lender should consider when presented with a loan request that will result in the change of ownership of a going concern include:

- Are the parties related?
- How did the parties arrive at the fair market value for the business; e.g., was an independent appraiser, or other acceptable method of evaluating a business used?
- What is the justification for the change of ownership? Will it benefit the small business?
- Is the repayment ability based, at least in part, on the historical performance of the business being acquired?

Asset Acquisition versus Stock Purchase

Where the change of ownership involves the acquisition of assets, the buyer does not assume the liabilities. Through a stock purchase, the buyer purchases the assets and assumes the liabilities. In both cases, the value of the business, including the value of the assets being acquired, must be established by an independent appraiser.

Partial Change in Ownership

When 7(a) loan proceeds are used for a change of ownership, the borrower must acquire 100 percent of the business. A partial change of ownership where the end result is that the borrower owns less than 100 percent of the business is not permitted.

Transactions Involving Family Members

Loan proceeds may be used in transactions between family members; however, the Lender must closely examine the business valuation, the company's historical performance documentation, and tax returns for accuracy.

Foreign-Owned Businesses or Non-U.S. Citizen-Owned Businesses

Foreign-owned Businesses (SOP 50-10(4), Sub A, Ch 2, ¶ 8(e), Page 31)

To be eligible, a foreign-owned applicant business must:

- Be located in the U.S.;
- Operate primarily in the U.S.
- Be authorized to operate in the state where it seeks SBA financial assistance;
- Pay taxes to the U.S.;
- Use loan proceeds exclusively for the benefit of the domestic operations.

Businesses Owned by Non-U.S. Citizens (SOP 50-10, Sub A, Ch 2, ¶ 15(h), Pages 70 & 70-1)

SBA can, in many cases, provide financial assistance to businesses owned by persons who are not U.S. citizens. SBA Form 912, "Statement of Personal History" identifies whether the owners and managers of the business are U.S. citizens. If they are not, they must provide documentation that includes their alien registration number. An alien registration number indicates that the person is in the U.S. legally. In addition, the Lender must:

1. **Obtain a photocopy of their INS documentation.** Lenders must place a photocopy of the individual's documentation in the case file.
2. **Verify the status of the documentation with the INS.** INS verification must be done as part of the loan application with the findings submitted with the application package. The lender must submit an INS Form G-845, "Document Verification Request", with supporting information to the nearest INS office. The response from the INS generally takes 6 weeks.

INS releases information about the status of an alien to lenders or other non-governmental entities ONLY when a signed and dated authorization from the alien is attached to and submitted with the Form G-845 on that alien. INS requires that authorizations provide the person's name, address, and date of birth. INS accepts either of the following authorization statements:

“I authorize the Immigration and Naturalization Service to release information regarding my immigration status to [name of lender], because I am applying for a U.S. Small Business Administration loan.” OR

“I authorize the Immigration and Naturalization Service to release alien verification information about me to [name of lender], because I am applying for a U.S. Small Business Administration loan.”

Without this additional language, INS will not respond to the Lender. It is also important not to abbreviate U.S. Small Business Administration. Individuals should submit the request on personal stationery, not SBA or lender letterhead. INS requires an original signature. Therefore, the Form G-845 and the statement authorizing INS to release the status information to the lender should never be faxed to an INS office.

3. **Determine if they are eligible based on their status.** For questions regarding status, Lenders should contact INS directly. A list of INS offices and sub-offices can be found at www.immigration.gov/graphics/fieldoffices/index.htm.

Legal Permanent Residents (LPR) are persons who may live and work in the U.S. for life unless the INS revokes this status through an administrative hearing. LPRs are eligible for SBA assistance. The primary document acceptable as evidence of LPR status is INS Form I-551 (551). INS has two versions of the 551. One is titled “Resident Alien Card”. The other is titled “Permanent Resident Card”. The latter is the most recent version of the 551. INS requires replacement of the 551 every 10 years to update the photograph. SBA requires that the 551 or an acceptable substitute must be current at the time it is submitted with an application.

INS revokes LPR status and deports aliens when they are convicted of criminal activity, normally a felony. Therefore, LPRs with felony convictions are not eligible unless:

- INS provides written documentation identifying the specific criminal activity stating that the LPR status is in good standing in spite of the specific documented activity, AND
- AA/FA or designee authorizes processing of this application.

Businesses owned by other documented aliens may be eligible. They must have current/valid INS documentation permitting them to reside in the U.S. legally. The documentation/status of each alien must be verified with INS.

4. **Determine if they will need to comply with the “Additional Requirements for Businesses owned by Foreign Nationals, Foreign Entities, and Non-Immigrant Aliens residing in the U.S” discussed below:**

Businesses at least 51% owned by individuals who have verified LPR Status from the INS and control the management and daily operations of the business can obtain financial assistance from SBA without complying with the “Additional Requirements” outlined in this section. Without verified LPR status, all businesses with foreign elements must also:

- Provide evidence that separate continual and consistent management (in addition to the owners) exists and will continue indefinitely.
- Have management that has U.S. citizenship or verified LPR status.
- Have management that has operated the business for at least 1 year prior to the application date.
- Pledge collateral within the jurisdiction of the U.S. sufficient to pay the loan in full any time during its life.

Miscellaneous Types of Businesses

Farms and Agricultural Businesses (SOP 50 1-(4), Sub A, Ch 2, ¶ 5, Page 22)

Farms and agricultural businesses are eligible for SBA business loan assistance but the Agency is not the primary maker or guarantor of loans to farms within the Federal government. Applications from businesses involved in raising crops or raising animals should first be referred to Rural Development (formerly Farmers Home Administration) programs, particularly if the applicant has a prior or existing relationship with that agency.

Medical Facilities (SOP 50 10(4), Sub A, Ch 2, ¶ 15(d), Page 68)

For profit hospitals, clinics, emergency outpatient facilities, medical and dental laboratories are eligible. Convalescent and nursing homes, i.e. Adult Living Facilities (ALF), **are eligible if** they are primarily involved in providing services, not just providing room and board, and they are licensed by the state where they will be located.

Litigation, Bankruptcy, Probation or Parole

Litigation (From Question 9 on SBA Form 4)

If a loan application discloses pending litigation, Lender should have the Borrower furnish the following:

- A copy of the complaint and answer that has been filed.
- An explanation from the Borrower’s counsel as to the nature and potential effect of the litigation on Borrower’s business.

Bankruptcy (From Question 10 on SBA Form 4)

If a loan application discloses a prior bankruptcy or that the applicant is currently in bankruptcy, Lender should have the Borrower furnish the following:

- An explanation from the Borrower as to the circumstances that caused the bankruptcy.
- If completed, a copy of the discharge.
- If ongoing, a copy of the plan, if any.

Probation or Parole (SOP 50-10(4), Sub A, Ch 2, ¶ 8(n), Pages 38 & 39)

Applications **will not** be accepted from businesses where a principal (any one of those required to submit an SBA Form 912, "Statement of Personal History"):

- is currently incarcerated, on parole, or on probation; or
- is a defendant in a criminal proceeding; or
- whose probation or parole is lifted expressly because it prohibits an SBA loan.

Affirmative response to Questions 7 or 8 on SBA Form 912: Eligibility judgments are made on a case-by-case evaluation of the nature, frequency, and timing of the offenses. An affirmative response does not necessarily preclude a loan to a business.

If yes to Question 7, the applicant must:

- Furnish details in a separate exhibit, including dates, location, fines, sentences, etc., whether misdemeanor or felony, dates of parole/probation, unpaid fines or penalties, names under which charged, and any other pertinent information.
- Complete a "Supplemental Affidavit to SBA Form 912, Statement of Personal History."

If yes to Question 8, the applicant must also furnish Fingerprint cards, Form FD 258 (available from the local SBA office) to be processed.

Fingerprint cards need to be submitted as soon as the requirement is identified to expedite loan processing.

The FBI will not process fingerprint cards with highlighted fields or fingerprint cards that have been perforated with any type of hole-puncher.

Combination Financing (sometimes referred to as Piggyback Financing) (SOP 50-10(4), Sub A, Ch 2, ¶ 4(g), Pages 20 to 23)- Amended by SBA Policy Notice 0000-1727.

Combination Financing occurs when a conventional non-SBA guaranteed commercial loan and a 7(a) loan are made to a single borrower at or about the same time and for the same or a similar purpose.

The SBA limits on the size of loans only applies to the 7(a) guaranteed loan. Therefore, the Combination Financing structure enables a lender to consider larger projects than could be considered with the 7(a) \$2,000,000 limit alone.

The legislation provides that Combination Financings must meet the following requirements:

- The financing must be comprised of both a loan guaranteed under the 7(a) loan program and a commercial loan which is not guaranteed by the federal government.
- The commercial loan may be made by the same participating lender that is making the 7(a) loan or by a different lender.
- The commercial loan may be made by a PLP lender.
- The commercial loan amount must not exceed the gross amount of the 7(a) loan.

If a PLP lender is making both the commercial loan and the 7(a) loan in a Combination Financing, the lender must submit the 7(a) loan to the SBA District Office, not the PLP Processing Center, for processing and approval.

Requirements Imposed on the Lender in the Senior Lien Position:

The lender must waive any provisions in its note or loan documents that:

1. Allow future advances except advances made for the reasonable costs of collection, maintenance, and protection of lender's senior lien.
2. Cross-collateralize the loan with other non-SBA financings provided by lender to borrower.
3. Have an early call feature.
4. Cause the note to be payable on demand unless the lender's note is in default.

In addition, if the note contains a default interest rate, a late payment charge, or a prepayment penalty, these must be subordinate to SBA's lien position on the collateral.

Note: If the commercial loan has a senior credit position to the 7(a) loan, a one-time fee equal to 0.7 percent of the amount of the commercial loan is to be paid to SBA. (See previous section on Fees.)

Other Requirements for Combination Financing

In addition to the items above, SBA has established the following requirements for Combination Loans:

- The term of the first lien note must be similar to the term of the SBA guaranteed loan, but no less than half the maturity of the SBA guaranteed loan.

- The first lien note must be fully amortizing and may not include a balloon payment.
- The interest rate of the first lien note may be no higher than the interest rate of the SBA guaranteed loan.
- A default interest rate on the first lien note is not permitted.
- No additional fees triggered by a default on the first lien note will be permitted.
- At least 75% of the proceeds of a Combination Financing must be used for real estate and long-term, fixed assets.
- The lien position for the SBA guaranteed loan may be no lower than second position.
- For the purpose of determining the size of the SBA loan, the “project” shall be defined as the total amount financed. It will not include the borrower’s down payment or any other items.
- The first lien note must be for a purpose that would be eligible for SBA financing.
- The lender cannot foreclose on the first lien note without foreclosing on the SBA note; therefore, there must be a cross default provision in both loan notes to ensure they are treated as one loan.
- Each of these items must be documented in the loan file to expedite review of the case.
- Please refer to SOP 50 10 (4) (E), Chapter 2 (Business Loan Eligibility), Paragraph 4 (Utilization of Personal Resources) (d) (3) through (9).

When the Combination Financing involves refinancing, the proceeds of both the guaranteed and non-guaranteed loans must both be eligible for SBA refinancing.

Once a Lender determines that the 7(a) applicant is eligible for SBA financial assistance, the next step is to determine if the applicant meets the credit standards of SBA.

Creditworthiness

Credit Analysis (SOP 50-10(4), Sub A, Ch 4, Pages 81 to 96)

SBA assumes that the Lender's decision to seek SBA's guaranty is made after the lender has conducted a thorough credit analysis of the applicant's request for financial assistance in accordance with prudent lending practices. **No loan can be guaranteed by SBA unless there is the reasonable assurance of repayment in a timely manner.**

The Lender's written credit analysis must demonstrate at a minimum a thorough assessment of 1) repayment ability; 2) financial statement analysis including ratio, trend, and pro forma analysis; 3) management capabilities; 4) collateral coverage; and 5) lender's experience with the applicant.

Collateral

Collateral is never a substitute for a full assessment by the Lender of the borrower's ability to repay the loan in a timely manner. If the Lender's analysis determines that the borrower lacks reasonable assurance of timely repayment from the earnings of the business, the loan request must be declined and not submitted to SBA for its guaranty.

In addition to a reasonable demonstration by the Lender of the applicant's ability to repay the loan timely, SBA has certain minimum collateral requirements. A 7(a) loan must be fully secured (or secured to the extent possible) with available collateral (both business and personal).

A loan is considered to meet SBA's collateral requirements if 1) the Lender obtains security interests in the available assets (business and personal) with a combined liquidation value that equals 100% of the loan approval (the Lender is not required to take liens on more collateral than is needed to secure 100% of the loan) or 2) the Lender obtains security interests in all available assets which together represents less than 100% of the loan amount. (Liquidation value of an asset means the amount expected to be realized if the lender sold the asset after conducting a reasonable search for a buyer and after deducting the costs of taking possession of the asset, preserving the asset and marketing the asset.) Although personal guaranties are not considered collateral, assets securing such guaranties are considered collateral.

When considering all assets available, the Lender should first consider assets acquired with the loan proceeds, then liens on other business assets, and then personal assets.

When loan proceeds will be used to buy business assets, the acquired assets must be pledged as collateral. When SBA refinances secured debts, SBA expects to have at least the same security as the original loan.

Commercial Real Property Collateral (SOP 50-10(4), Sub A, Ch 5, ¶ 3, Page 101)

If the purpose of the 7(a) loan is to acquire commercial real property, an appraisal for that property by a state licensed or certified appraiser is required when the approved loan amount (gross amount) exceeds \$250,000.

Appraisals are generally not required on secondary collateral.

Environmental Investigation and Mitigating Risk of Environmental Contamination
(SOP 50-10, Sub A, Ch 5, ¶ 7, Pages 115 to 128)

If the 7(a) loan is secured by commercial real estate, an environmental assessment in compliance with SBA's environmental policy must be done to determine any risk of liability for environmental contamination.

The Authorization must contain terms and conditions complying with the SOP requirement of an adequate and prudent investigation of the environmental risk (the "Environmental Investigation") on all Primary Collateral offered as security for any SBA-guaranteed loan. "Primary Collateral" is any business real property acquired or improved with loan proceeds or business real property pledged that represents over 50% of the value of all collateral securing the loan. If the Environmental Investigation determines potential existence of contamination, Lender must take adequate and prudent steps to mitigate the risks of contamination or Lender must decline the loan.

On 7(a) loans, SBA is responsible for determining the adequacy of the Environmental Investigation and the risk mitigation efforts. On PLP and *SBAExpress* loans, this responsibility falls upon the Lender. In addition to the SOP provisions, Lender's due diligence and risk mitigation are subject to normal prudent lending and commercially reasonable standards.

Although SOP 50-10 (4) addresses performance of environmental analysis prior to "disbursement," conducting the investigation and taking risk mitigation efforts can be time-consuming. SBA strongly advises Lenders to investigate and resolve environmental concerns early on, well before loan closing. For example, if an indemnification agreement is required from the seller, lengthy negotiations can occur, and the seller will be far more likely to provide indemnification prior to execution of sale documents at the closing.

Under the SOP's Environmental Procedures, the Lender (in PLP and *SBAExpress* loans) or SBA (all other 7(a) loans) must take the following steps:

1. Insert as necessary the certifications set forth in the Additional Conditions Section, paragraph 9 in the Boilerplate 7(a) Loan Authorization.
2. Insert the relevant environmental terms and conditions in the Loan Authorization (see Additional Conditions Section, paragraph 2 in Boilerplate 7(a) Loan Authorization).
3. Perform an adequate and prudent Environmental Investigation on all Primary Collateral.

The Environmental Investigation must consist of one or more of the following:

- A Transaction Screening Analysis (TSA). The SOP generally requires, at a minimum, performance of a TSA, which includes:
 - (1) Completion of Environmental Questionnaire (EQ) asking questions about past use of the property of seller and/or current operator and signed by seller or current operator; Lenders can use the American Society of Testing and Materials (ASTM) version or its own questionnaire if it is more expansive than the SBA questionnaire in SOP 50-10 (4).
 - (2) Site inspection by lender or lender's agent (not by seller or seller's agent);
 - (3) An Environmental Records Review (See Pars. 7.b (14), 7.d(2)), which includes:
 - (a) review of regulatory agency files to minimum search distances from site
 - (b) review of historical records showing past use of site
 - (c) Lender's recommendation regarding the need for further investigation
 - For loans of under \$25,000 or other limited exceptions, only an EQ is needed (See Par. 7d). The limited exceptions are:
 - (1) Site is vacant land with no prior business or agricultural use; or
 - (2) R/E collateral is only part of a multi-unit building; or
 - (3) Phase I done within 1 year from date of loan application, and:
 - (a) No risk of contamination at site, or
 - (b) Contamination found but no remediation required or remediation has been completed and "no further action" letter has been issued; or
 - (4) Lender has affirmative knowledge or belief (based on prudent lending standards) that property is not contaminated (Lender cannot rely upon the EQ to obtain this knowledge).
 - A Phase I Environmental Site Assessment (ESA) performed by an environmental professional is required if lending experience or other information suggests a reasonable likelihood that the past uses of the site or adjacent sites are subject to potential contamination. A Phase I ESA includes:
 - (1) Visual inspection of site and adjacent sites by environmental contractor.
 - (2) An Environmental Records Review (see above).
 - (3) Interviews with current owner and operators, neighboring sites, etc.
 - (4) Environmental contractor's recommendation re: need for further investigation.
4. Verify that the risk from any adverse findings is sufficiently mitigated to allow disbursement to occur. Disbursement is only justified if one of the following exists:
- The contamination does not exceed state action levels (Par. 7.g).
 - If more significant contamination has occurred, that the responsible governmental agency overseeing any cleanup has issued a "no-further action" letter (Par. 7.g).
 - If neither of the above applies, the seller or responsible party executes an indemnification agreement and can demonstrate that it has financial resources to complete the clean-up (Par. 7h). SOP 50-10 (4) contains a standard SBA indemnification agreement, which lenders can use without SBA approval.

Deviations from this agreement require approval of the SBA's Office of Litigation, Office of General Counsel. TIP: SBA has negotiated indemnification agreements with a number of large companies, including many oil companies. Lenders should check with their local District or Branch office if a seller is not willing to sign the standard SBA form.

- If indemnification is not available, the loan can only go forward if allowed under the risk mitigation factors outlined in SOP 50-10 (4), par. 7i. TIP: Generally, if remediation is ongoing and the amount of contamination is other than negligible, disbursement is discouraged unless there is either environmental insurance or escrow of funds from the sale of the property to cover reasonably anticipated clean-up costs.

5. Lender must document its decision-making and the actions it took to address environmental concerns and to justify approval and disbursement for the loan and retain these documents in the loan file.

SBAExpress loans: An *SBAExpress* lender may not request an *SBAExpress* loan number for a loan that will have Primary Collateral that will not meet SBA's environmental requirements or that will require use of a non-standard indemnification agreement.

CHAPTER 2 - LOAN CLOSING

This chapter provides the Lender with guidance on closing and disbursing 7(a) loans in compliance with SBA requirements. It explains SBA's requirements by reviewing the 7(a) Loan Authorization Boilerplate and pointing out what Lenders should be looking for at the time of closing to avoid problems later.

The general requirements a Lender must meet for SBA to guaranty 7(a) loans are described, in part, in the SBA Form 750, Guaranty Agreement. The Authorization provides specific requirements for each 7(a) loan. Lenders are expected to close 7(a) loans in the same manner in which they close non-SBA loans. Lenders are responsible for knowing how to properly close loans, secure collateral, obtain and perfect the required lien positions, and meet other authorization requirements.

SBA relies on representations in the loan application and supporting documents in issuing the Authorization. **The SBA guaranty is contingent upon the Lender:**

1. Complying with the SBA Loan Guaranty Agreement, SBA Form 750 (SBA Form 750B for short-term loans) and any other required supplemental guaranty agreements between Lender and SBA;
2. Paying the guaranty fee in a timely manner;
3. Complying with current regulations and SOPs;
4. Having no evidence of unremedied adverse change that would prevent disbursement;
5. Satisfying all the conditions of the Authorization; and
6. Making timely disbursement.

Three of the most common deficiencies leading SBA to recommend a cancellation, denial or repair of its guaranty (at the time the lender requests that SBA honor its guaranty) happen at loan closing:

1. Unauthorized, improper, uncontrolled, or undocumented disbursement of loan proceeds.
2. Failure to obtain or adequately document a required equity injection.
3. Failure to obtain required collateral or properly perfect lien position.

Closing also is the last time the Lender has an opportunity to discover eligibility and credit problems before the Lender disburses the loan.

GUARANTY FEE PAYMENT

Lenders must send the guaranty fee payment to SBA's Denver Finance Center, not the SBA processing office. The address is in the Authorization.

Be sure the initial disbursement is substantially more than the amount needed to cover the guaranty fee. No disbursement can be made solely to recover the guaranty fee. It must be part of another disbursement for other loan purposes.

For loans of \$150,000 or less, the Lender can retain 25% of the fee. (Note: Lenders should keep the 25% of the fee and send the 75% to SBA's Denver Finance Center. Do not send the entire amount to Denver and wait for a refund. Lender may keep this 25% or refund it to the Borrower.)

Guaranty Fee Due date

For loans with terms greater than 12 months, the guaranty fee is due to SBA within 90 days of the date of loan approval. For loans with terms of 12 months or less, Lender must pay this fee at the time of application. **SBA will not extend or waive the due date for payment of the guaranty fee. If the fee is not received within the required time period, the guaranty will be cancelled.**

Fees Associated with Loan Increases

If the loan amount increases, an additional guaranty fee is due within the original 90-day timeframe; however, if the original guaranty fee has already been paid and 90 days have passed since the approval date, the additional fee must be submitted by the Lender with the request for the increase.

Refunds of Guaranty Fees

- If there has been no disbursement – **Full refund**
(Lender must request cancellation of loan and return of guaranty fee. The refunded fee is paid to the Lender, not the Borrower.)
- If there has been any disbursement - **No refund**
- If the Lender already has paid the guaranty fee and then reduces the loan amount after making an initial disbursement - **No refund.**

Guaranty Fees for Two Loans Approved within 90 days

If two loans each with a maturity of 12 or more months are approved for the same Borrower within 90 days, the guaranty fee calculation on the second loan will be based on the **combined loan size and guaranty percentages**. The first loan will have a guaranty fee equal to the amount that would be due if ONLY that loan was being made. The guaranty fee will be adjusted on the second loan.

LOAN AUTHORIZATION

After SBA approves the loan guaranty, an Authorization will be issued for the loan using the required language in the National 7(a) Authorization Boilerplate (Boilerplate). The Authorization is not a loan agreement. It is a contract between the Lender and SBA, who each sign the Authorization, indicating specific conditions which must be met for SBA to provide a guaranty on a loan made by the Lender to a Borrower. The requirements of the Authorization are directed to the Lender not the Borrower, and the Borrower does not sign the Authorization

Lenders are responsible for complying with SBA requirements to keep the SBA guaranty in force, and the Authorization emphasizes this SBA policy.

The Boilerplate may be found at and downloaded from <http://www.sba.gov/banking/national/#Boilerplate> . The Boilerplate is SBA's national standard. No regional, state, or local loan authorization boilerplate language may be used in place of the Boilerplate, and the language in the Boilerplate MUST NOT be altered.

The Boilerplate is also an excellent reference document. References to the specific regulations, standard operating procedures (SOPs) and Notices that relate to each section are contained in gray boxes above each section. Therefore, SOP references will appear in this chapter only for items not found in the Boilerplate.

The Boilerplate has been programmed as a Word Wizard for use by SBA in creating Authorizations ("Wizard"). Lenders are encouraged to use the Wizard, but are not required to use it, and may automate the Boilerplate in other software if they choose. (Use of any other automation tools does not relieve Lenders from their responsibility to ensure that the Authorizations they create comply with the Boilerplate.)

The Boilerplate's nine separate sections:

- A. Guaranty Fee
- B. Servicing Fee
- C. Lender Requirements
- D. SBA Forms
- E. Lender Contingencies
- F. Note
- G. Use of Proceeds
- H. Collateral
- I. Additional Conditions

The Wizard's six separate sections:

- 1. Loan Information includes Boilerplate sections A.-E.;
- 2. Repayment Terms includes Boilerplate section F.;
- 3. Use of proceeds includes Boilerplate section G.;
- 4. Collateral includes Boilerplate section H.;

5. Additional Conditions I & II includes Boilerplate section I.

The Boilerplate reflects current SBA policy and is considered an appendix to SOP 50-10. It is updated as necessary to reflect policy changes in subsequent regulations, notices or SOP modifications. The Wizard also is updated as necessary to correct technical problems or upgrade the programming used. Updated Boilerplates are issued by Notice and replace all prior versions. Updates to the Boilerplate are available on SBA's banking website (www.sba.gov/banking).

When SBA releases a new version, Lenders have a **30-day grace period** to begin using the new version. The Wizard prints the version number in the footer of each Authorization; it also can be viewed by selecting the "About 7(a) Wizard" option in the Wizard menu.

PLP Lenders processing their own PLP loans must prepare an Authorization at the time of loan approval. PLP Lenders sign the Authorization on behalf of both the Lender and SBA, and then send it to the appropriate SBA Commercial Loan Servicing Center. When preparing the Authorization, a PLP Lender may develop an Authorization condition not pre-approved in the Boilerplate without SBA approval, if necessary, for that particular loan, *provided* Lender uses it *only 1 time*. Conditions to be used on multiple loans require SBA approval. PLP Lenders also have authority to make certain unilateral changes to the Authorization, which Lender should document with a modification letter or memorandum in order to create a paper trail of changes from approval date through closing date. Other lenders must seek SBA approval of changes to the Authorization.

Suggestions to improve the Boilerplate or to include new provisions may be sent to Auth-7a@sba.gov. The Authorization committee will consider suggested changes during the review and updating process.

SBA Loan Number

SBA issues this number when SBA approves and funds the loan. This number never changes and should appear on all closing documents and any correspondence Lender has with SBA related to the loan.

SBA Loan Name

The SBA Loan Name is the first available name from this list:

- DBA of Operating Company (OC)
- Name of OC
- DBA of Borrower
- Name of Borrower

In the case of multiple Borrowers or OCs, apply the same rule, using the first OC or Borrower listed in the Authorization. (Note: The Wizard automatically selects the SBA Loan Name based on the Borrower and OC information provided.)

The SBA Loan Name may change if there is a change in OC or Borrower name or DBA from the time of application to the time of closing. Notify SBA of any changes, so the Lender's and SBA's records are consistent.

Received date

SBA requires the inclusion of a "received date" to facilitate interest rate calculations on variable rate loans. For loans processed by SBA, upon receiving all necessary documents, the SBA processing office stamps every application "received" on the date it arrives at SBA. For PLP loans, the "received" date is the date the Lender's request for the loan number is "received" by SBA in an acceptable form, not the "approved date".

Borrower information

SBA allows single Borrowers, Co-Borrowers, and multiple Borrowers in the 7(a) program. All requirements of the Authorization which refer to Borrower also apply to any Co-Borrower.

Multiple Borrowers – Lender may make a single 7(a) loan to multiple Borrowers (however, multiple EPCs are not allowed), provided each business is a co-obligor and anyone owning 20% or more of any of the applicant businesses is a Guarantor.

Eligible Passive Companies and Operating Companies (EPC/OC) – SBA allows a loan structure where the Borrower is a passive owner of the assets to be financed with the loan proceeds and leases the assets to an "Operating Company" (OC). The Borrower in these cases is called an "Eligible Passive Company" (EPC).

When using the Wizard, if the loan is structured as an EPC/OC loan, check the box on the Wizard indicating that the Borrower is an EPC. (If the OC is shown as a Co-Borrower only, the Authorization will not contain the assignment of rents provision required for EPC/OC loans in the collateral section and will not reference the requirements that apply to both Borrowers and OC in the rest of the Authorization.)

Lender Responsibilities

The Authorization for each loan lists the specific conditions which must be met by the Lender for SBA to guaranty the loan. The Authorization does not outline what action the Lender must take to satisfy those conditions. SBA expects the Lender to know that it must:

- Prepare all necessary loan documents and have those documents signed by the appropriate individual(s), including spouses when necessary
- Perfect security interests (liens) in any collateral specified in the Authorization in accordance with applicable federal or state law
- Obtain evidence in the form of title insurance or reports or UCC lien searches that show the Lender obtained the specified lien position against all required collateral
- Disburse loan proceeds for only those purposes specified in the Authorization
- Retain evidence of how it complied with each condition set forth in the Authorization

Disbursement dates

The Lender may establish its own disbursement schedule as long as all loan proceeds are disbursed within 24 months after the date of the approval.

Note Terms

Maturity:

The Lender may calculate the loan maturity date from either the date of the Note or the date of initial disbursement. Remember, if there is a change in the use of proceeds between the date that the loan is approved and the date that the Lender is ready to close the loan, the maturity date may have to be re-calculated and changes made to the Authorization.

Repayment terms:

The repayment terms inserted onto the SBA Note must be EXACTLY the same as those Boilerplate conditions that appear in the Authorization. The Lender must not replace or supplement the repayment terms in the Boilerplate or Authorization with Lender-specific language. If there is a need for a specific term for a particular loan that is not in the Boilerplate, the Lender must obtain approval from SBA.

State-specific language:

Check the Authorization to ensure any necessary state-specific options have been inserted. If the Borrower moved to another state subsequent to loan approval, check to see that any necessary state-specific provisions that relate to the Borrower's new state of residence are added to the Authorization and loan documents.

Prepayment charges:

Every Authorization contains prepayment language that must be inserted into the Repayment Terms section of the Note, as follows:

For loans sold on the secondary market-

- Borrower may prepay up to 20% of balance at any time without charge
- For a prepayment of over 20%:
 1. Borrower must give Lender three weeks written notice or pay 21 days of interest
 2. Borrower must prepay within 30 days of notice date or provide Lender new notice.

For loans with a maturity of 15 or more years-

The Authorization must contain an additional prepayment fee, called a "subsidy recoupment fee." This fee applies where the Borrower voluntarily prepays a loan; the prepayment amount

exceeds 25% of the outstanding balance of the loan; and the prepayment is made within 3 years after first disbursement (not approval) of the loan proceeds. The fee calculation is as follows:

- During the first year after disbursement, 5% of the amount of the total prepayment; During the second year after disbursement, 3% of the amount of the total prepayment, and
- During the third year after disbursement, 1% of the amount of the total prepayment.

The Wizard automatically adds this provision for loans with maturities exceeding 15 years.

Use of Proceeds

The Boilerplate contains 25 specific “Use of Proceeds Options”. Lender can make one loan with several different use of proceeds provisions.

Lender must not include items to be paid by Borrower’s equity injection or other funds not related to the SBA loan in this section of the Authorization List only how loan funds are to be used.

Lender may not disburse loans funds solely to pay the guaranty fee. Lender may disburse, as working capital only, funds not spent for the purposes specifically stated in the Authorization if such funds do not exceed 10% of such specific purposes, or \$10,000, whichever is less. An EPC must not receive any working capital.

Restrictions on Use of Proceeds

Loan funds may not be paid to principals or associates of the Borrower including reimbursement for funds the Borrower already used.

Loan funds may not be used for floor plan financing.

Loan funds must benefit the business Borrower or Operating Company.

Loan funds may not be used to pay delinquent IRS withholding taxes, sales taxes, or other similar funds held in trust.

If the business has used operating capital to purchase hard assets, then those funds may, *with proper documentation*, be reimbursed to the business (not the owner) from SBA loan proceeds.

Equity injection

Lenders should document equity injection at the same time they document the use of proceeds – **at closing. The Lender must not disburse a loan until it has proof of any required equity injection.**

Proper evidence of a Borrower’s equity injection may include the copy of a check together with proof it was processed or a copy of an escrow settlement sheet with a bank account statement

showing the injection into the business prior to disbursement. A promissory note, “gift letter,” or financial statement generally are not sufficient evidence.

Lack of proper and complete documentation of an equity injection required in the Authorization is one of the most common reasons for a reduction or denial of SBA’s guaranty at the time of purchase. If a Lender overlooks this requirement at the time of closing, the Lender usually finds it very difficult to adequately document equity injection at a later date.

Collateral

The Lender is expected to know what documents and procedures are necessary to obtain and perfect an enforceable security interest or lien in each class of collateral identified in the Authorization.

Federal law language

The following language must appear in all lien instruments including Mortgages, Deeds of Trust, and Security Agreements:

“The Loan secured by this lien was made under a United States Small Business Administration (SBA) nationwide program which uses tax dollars to assist small business owners. If the United States is seeking to enforce this document, then under SBA regulations:

- a) When SBA is the holder of the Note, this document and all documents evidencing or securing this Loan will be construed in accordance with federal law.
- b) Lender or SBA may use local or state procedures for purposes such as filing papers, recording documents, giving notice, foreclosing liens, and other purposes. By using these procedures, SBA does not waive any federal immunity from local or state control, penalty, tax or liability. No Borrower or Guarantor may claim or assert against SBA any local or state law to deny any obligation of Borrower, or defeat any claim of SBA with respect to this Loan.

Any clause in this document requiring arbitration is not enforceable when SBA is the holder of the Note secured by this instrument.”

State-specific requirements

The Authorization lists any state-specific language that must be inserted in the Guaranty or other loan documents if the Guarantor or Borrower resides in that state. If a Borrower or Guarantor moves to a different state before loan closing, Lender must follow any appropriate state-specific requirements and must add such requirements to the Authorization and any other documents required, before loan closing.

Additional Requirements

Prior to initial disbursement, the Lender must ensure that the Borrower has obtained appropriate insurance coverage, as described below. The Lender also must ensure that the insurance remains in effect for the life of the loan:

Flood insurance:

The Lender must require Borrower to obtain Federal flood insurance, or other appropriate hazard insurance, if FEMA (Form 81-93) indicates that any portion of the collateral, including personal property, is or will be located in a special flood hazard zone. The amount of flood insurance must be the lesser of the insurable value of the property or the maximum limit of coverage available, and the policy must contain a MORTGAGEE CLAUSE/LENDER'S LOSS PAYABLE CLAUSE (or equivalent), in favor of Lender. Borrowers who fail to maintain required flood insurance for the term of the loan are ineligible for future SBA assistance. The only exception is when flood insurance required for personal property collateral cannot be obtained or is prohibitively expensive. In such cases, the Lender must ask SBA for the waiver in writing and explain the circumstances.

Hazard insurance:

Borrower must insure real estate and personal property, including machinery, equipment, furniture, fixtures and inventory, that is loan collateral in an amount equal to its full replacement cost. Where Borrower is unable to insure the property at its replacement cost, coverage must be for the maximum insurable value. The insurance policy must provide for at least 10 days written notice to Lender prior to policy cancellation, and contain a MORTGAGEE CLAUSE/LENDER'S LOSS PAYABLE CLAUSE (or equivalent), in favor of Lender, and state that any act or neglect of the mortgagor or owner or the insured property will not invalidate the insurable interest of the Lender.

Life or disability insurance:

Life insurance and/or disability insurance is not required for all loans, but the Lender should require life or disability insurance where there is a concern over whether the business could survive in the absence of an individual or small group of individuals that provide the management for the small business concern. When life or disability insurance is deemed prudent, the Lender may accept a COLLATERAL ASSIGNMENT of an existing or new decreasing term or universal life insurance policy. LENDER SHOULD NOT BE NAMED AS A BENEFICIARY.

Workers' compensation insurance:

Borrower is required to obtain workers' compensation coverage in full compliance with state law.

Other insurance:

The Lender may require the Borrower to obtain additional insurance, including liability insurance, product liability insurance, dram shop/host liquor liability insurance, malpractice insurance, or other state-specific insurance requirements, depending on the nature of the business obtaining the loan and the risk Lender perceives.

Environmental Investigation and Certifications

SBA requires that, prior to loan closing and disbursement, the Lender conduct an adequate Environmental Investigation and take steps to mitigate the liability associated with the risk of environmental contamination on all primary collateral offered as security for any SBA-guaranteed loan. See Chapter 1 of this Guide for more details. Prior to loan closing, Lender must obtain all certifications set forth in paragraph 9 of the Boilerplate regarding environmental contamination.

Borrower, Guarantor and Operating Company Documents

Different documents are required for the different types of legal entities (for example, corporations, sole proprietorships, partnerships, limited liability companies, and limited liability partnerships). Several common types of legal structures and their required documents are listed in the Authorization. This list provides Lenders with general guidance on the documents required for the various types of entities, and accommodates changes in organization structure that may be made before closing. Lenders must notify SBA of any changes to Borrower's or Operating Company's structure or organization, and must submit material changes to the Authorization for SBA approval.

This section also contains requirements for the small business concern's trade name registration, evidence that ownership and management have not changed without Lender's approval and some additional optional paragraphs.

Operating Information

Tax return verification and SBA/IRS Form 4506T

SBA requires Lenders to verify the accuracy of financial information being relied on for the credit and eligibility determination. The only exceptions to this requirement are (i) for start-up companies (who have no financial information to verify) and (ii) for Guarantors. (Note: If the transaction involves a change of ownership, verification of the seller's financial information is required.)

The Lender must use an SBA/IRS Form 4506T to request a transcript, not a copy, of the tax return. The transcript provided by IRS is a line by line summary. (Partnership and corporate returns are not transcribed in full but are rather covered in a form letter containing limited financial data.) To expedite the loan application process, Lenders are advised to submit Form

4506T as soon as possible in the application process. Ordinarily, IRS responds within two weeks.

Upon receipt of the IRS transcript, the Lender must compare it with the financial statements that the Borrower submitted prior to any disbursement. If there is a significant discrepancy, the Lender must notify SBA and not disburse any loan proceeds until the discrepancy is resolved. If that happens, the Lender can inform the applicant that SBA halted disbursement while it investigates an adverse change but the Lender may not refer to the IRS verification specifically. SBA may deny liability on its guaranty to any Lender who disburses any proceeds whatsoever before receiving a response (or after receiving a response but before a discrepancy is resolved).

If the IRS has not responded within 10 business days from the time Lender submitted the 4506T, Lender may disburse the loan but still must obtain a response from the IRS, by resubmission of the 4506T if necessary, and must conduct the necessary comparison.

Authority to conduct business

The Lender must obtain evidence of the Borrower's Employer Identification Number (EIN) and any permits, licenses, insurance or other approvals necessary for the Borrower to lawfully operate the business. For example, if the Borrower is an attorney, engineer or doctor, the Lender is required to obtain a copy of the license required by the state.

Other Possible Requirements

Agreement of franchisor

This agreement includes access to the franchisor's books, 30 days notice to Lender of intent to terminate the franchise agreement giving the Lender an opportunity to cure, and deferral of franchise fee payments if loan goes into default. If these requirements cannot be met, they can be waived if there are only minimal credit effects from not having these agreements.

Change of ownership

A stock purchase may be used to effectuate a change of ownership in a going concern. This method may be used where (1) the corporation redeems or repurchases all outstanding shares from existing shareholders, or (2) a third party buyer purchases all outstanding shares from existing shareholders. In either case, certain documentation is required at loan closing:

- The buyer(s) and corporation must sign the note;
- The principals of the buyer will be required to guaranty the loan; and
- The Lender should obtain an opinion from the Borrower's or Lender's counsel that the transaction complies with state law and specifying that adequate consideration exists and that the corporation cannot deny liability for the debt for failure of consideration.

Appraisals

The Authorization may require an appraisal of real estate or equipment. An appraisal is not required for real estate pledged as collateral but not financed by the SBA loan, unless the real estate is the “primary collateral” for the loan. Real estate is considered “primary collateral” for loans where the assets being financed provide less than 50% collateral coverage.

Appraisers must be:

- Independent and have no direct or indirect, financial or other interest in the property being appraised or the loan transaction.
- Capable of rendering an unbiased opinion.
- Hired and paid by the Lender, not the Borrower or the seller of the property or business. State certified or licensed in accordance with the Uniform Standards of Professional Appraisal Practice (USPAP).

A Lender may accept a SELF-CONTAINED APPRAISAL REPORT or a SUMMARY APPRAISAL REPORT however, a RESTRICTED APPRAISAL REPORT is never acceptable for an SBA-guaranteed loan. An acceptable appraisal will:

- Identify and describe the real property
- Identify the interest being appraised and include the legal description and known encumbrances
- State the purpose and intended use of the appraisal
- Define the value (cost, income or comparable sales) to be estimated
- State the dates of the appraisal and report
- Identify all assumptions and limiting conditions
- Specify how data was collected and reported
- Describe the information considered, procedures followed, analysis, opinions and conclusion
- Provide the appraiser’s opinion of highest and best use, when appropriate
- Explain the exclusion of any usual valuation method
- Provide any additional information that may be appropriate
- Have the signature and certification of the appraiser and include a disclosure by the appraiser of any involvement or relationship with the owner.

Special Provisions When the Loan Covers Construction

Earthquake provision

When loan proceeds are used to construct a new building or to construct an addition to or renovate an existing building, the Authorization will include a provision entitled “Building Standards,” which requires the Lender to comply with Presidential Executive Order 12699 “Seismic Safety of Federal and Federally Assisted or Regulated New Building Construction”. The Lender must comply with this requirement even if the construction project is not located in an area historically known for earthquake activity.

This means that all construction must comply with either the standards published by the National Earthquake Hazards Reduction Program's "Recommended Provisions for the Development of Seismic Regulations for New Buildings" (NEHRP) or one of these alternative standards:

- 1991 Uniform Building Code of the International Congress of Building Officials (ICBO);
- 1992 Supplement to the Building Officials and Code Administrators (BOCA) National Building Code; or
- 1992 Amendments to the Southern Building Code Congress (SBCC) Standard Building Code.

Lenders must obtain a certification from a licensed architect, construction engineer, or similar professional, or a local or state agency responsible for building code enforcement, stating that the construction complies with the NEHRP standards or one of the alternative standards.

General construction loan requirements

These provisions are intended to ensure quality construction and reduce the risk to both the Lender and the Borrower should the loan proceeds allocated to the construction turn out to be insufficient to cover the full cost of construction. Generally, Lender may not allow the Borrower to act as its own general contractor (SOP 50-10 (4)(B), Subpart A, Chapter 5, paragraph 6(e)(2), page 110).

Lender must:

- Obtain evidence of the Borrower's ability to pay cost overruns,
- Make regular inspections to ensure that construction conforms to plans,
- Obtain evidence that the completed building will meet all necessary codes and permits requirements,
- Obtain properly executed Forms 601,
- Obtain lien waivers or releases, and
- Take all safeguards appropriate to construction loans.

When building inspections are required as a condition before disbursing additional proceeds, the inspections must be conducted by a qualified individual. Inspections by Lenders are not sufficient and do not comply with SBA's requirements.

SBA Form 601 is required by federal civil rights laws when proceeds of more than \$10,000 are used for construction. This form, known as the "Agreement of Compliance", is a certification that the contractor has complied with anti-discrimination laws. Both the contractor and the Borrower must execute the SBA Form 601 no later than the loan closing. SBA Form 601 is not required when SBA-guaranteed funds are used to refinance interim debt.

Bond requirement

SBA requires a 100% payment and performance bond and builder's risk insurance for any 7(a) loans where more than \$125,000 in SBA-guaranteed proceeds are used to directly finance

construction. This is to ensure that the construction will be completed if the construction contractor fails to do so.

SBA will consider waiving this requirement if the Lender meets certain strict conditions. In general, the Lender must provide proper documentation of the project and very closely monitor the disbursement of loan proceeds. This includes using construction mortgages and lien waivers to protect the Lender and SBA and place their legal claims ahead of all others. In addition, Lender must document that the Borrower made any required equity contribution to pay for the early stages of construction. PLP Lenders have the authority to grant this waiver provided that the Lender documents the waiver in writing and places the documentation in the loan file.

No bond is required if SBA-guaranteed loan proceeds are being used solely to refinance interim construction debt and SBA is not guaranteeing that interim debt—sometimes known as “takeout” financing. In this case, there is no need for the protection provided by a bond because the risk is being “assumed” by the interim Lender and SBA funds are not involved until after the construction is completed.

Additional requirements when construction financing exceeds \$125,000

In addition to the bond and insurance provisions discussed above, SBA imposes certain documentation requirements on the Lender if the SBA-guaranteed portion of construction financing exceeds \$125,000. For example, the Lender is required to obtain a copy of the Borrower’s construction contract which must not exceed a specified price. The Authorization will specify provisions that must be in the construction contract with regard to the Borrower requesting or agreeing to material changes in the plans. If the Borrower is putting its own funds into the construction project, the Lender must have evidence that it has done so before disbursing any SBA-guaranteed loan funds.

Requirements When the 7(a) Loan is the Take-out Financing for a Construction Loan

When the 7(a) loan is not used for construction financing, the Lender still has certain documentation obligations. Either prior to the 7(a) loan closing or at the closing, the Lender must have evidence that several conditions have been met. These conditions include: that the construction has been substantially completed; the project has been paid-in-full; and that no unpaid labor or materialmen’s liens (such as a mechanic’s lien) exist. Other conditions are listed in the Authorization under the heading, “Construction Financing without SBA Guaranty.”

Borrower’s Certifications

As part of the terms and conditions of the Authorization, the Lender must obtain certain certifications and agreements from the Borrower and the Operating Company prior to disbursement of loan proceeds. These certifications are generally found in paragraph 9 of Section I (Additional Conditions) of the Authorization.

Mandatory certifications required from Borrower and Operating Company

The following certifications are required for all Authorizations:

- Receipt of Authorization
- Child Support
- Current Taxes
- Environmental
- Reimbursable Expenses
- Book, Records, and Reports
- Equal Opportunity
- American-made Products
- Taxes
- Distributions
- Ownership Changes
- Transfer of Assets

Additional certifications from Borrower and Operating Company

The Authorization provides for additional certifications from Borrower and Operating Company, concerning fixed assets, location, and salary limitations and occupancy. Limitations on acquiring fixed assets, new locations, and withdrawals and salaries are imposed only when necessary for the protection of SBA. Occupancy certifications are required when loan proceeds are used for the purchase or renovation of an existing building or construction of a new building.

Sample Borrower's Certification

The sample form in Appendix D of the Boilerplate, Borrower's Certification (3 pages), is a compilation of the various certifications found in the Boilerplate and provides a space for the Borrower to initial next to those certifications applicable to the particular loan. Lenders must retain an executed document containing these certifications, and may use this sample form as a basis for that document or for incorporating the required certifications into their loan agreement (if Lender uses one). The certifications, not the form, are required. Lenders may create and use their own certification form.

Sample Loan Agreement

SBA does not require a separate loan agreement to be signed by the Borrower. If it is the Lender's custom to require a loan agreement, it may do so. The Lender may use its own form of loan agreement or it may use the sample SBA form found in Appendix D of the Boilerplate.

Required SBA Forms for Closings

With the exception of SBAExpress loans, Lenders must use the SBA forms listed in Section D of the Authorization. Substitutions are not allowed. Lenders may use computer-generated versions of mandatory SBA Forms, as long as they are exact reproductions. These forms are:

- Note, SBA Form 147, version 4.1
- Guaranty, SBA Form 148
- Limited Guaranty, SBA Form 148L
- Settlement Sheet, SBA Form 1050
- Compensation Agreement, SBA Form 159
- Agreement of Compliance, SBA Form 601
- Equal Employment Opportunity Poster, SBA Form 722
- Notice to New SBA Borrowers, SBA Form 793
- Tax Return Verification, SBA/IRS Form 4506T

The Wizard will automatically insert into the Authorization a list of required forms, as applicable.

The Authorization contains the information needed to complete these forms. SBA Forms and Instructions can be found at www.sba.gov/banking.

Note, SBA Form 147

Lenders must use SBA Form 147, Version 4.1, and must follow the instructions accompanying the form on how to complete the form.

In the Information Grid at the top of the Note, Lenders must insert information as follows:

- SBA Loan Number and SBA Loan Name: same as stated in the Authorization; name must match signature block
- Date: the date the Note will be signed
- Loan Amount: principal amount
- Interest Rate:
 1. Fixed rate loans – insert the actual fixed rate, for example “10%”
 2. Variable rate loans – insert “variable rate” or “P+2%”
- Borrower:
 1. Insert ALL Borrower names
 2. No DBAs
- Operating Company:
 1. Applicable only if EPC structure
 2. Insert Operating Company name
 3. No DBAs

The “SBA Loan Name” and the “Borrower” are not usually the same. Under the SBA Loan Name convention, the Borrower Name is the last option for the SBA Loan Name. If any of the names have changed from the time the loan was approved, the Lender must notify SBA as well as document the changes on the Authorization.

Remember:

- Repayment terms must match the Authorization exactly.
- Check for state-specific terms in the Repayment section and the Collateral section of the Authorization.

Guaranty, SBA Forms 148 and 148L

The Authorization will indicate whether repayment of the loan must be guaranteed by specific individuals or specific legal entities, such as corporations, trusts, or partnerships. Whenever the Authorization requires Guaranties, the Lender must use SBA Form 148, Unconditional Guaranty, or SBA Form 148L, Limited Unconditional Guaranty, and must follow the instructions accompanying the form on how to complete the form. The use of this form ensures nationwide consistency in court decisions interpreting the enforceability of the guaranty against guarantors of SBA loans.

The Authorization will indicate whether a Guaranty must be full or limited. SBA Form 148 is used whenever the Guarantor is liable for repayment of the entire amount of the Borrower’s loan. SBA Form 148L is used whenever the Lender intends to limit the scope of the Guarantor’s liability, such as limiting the amount or duration of the Guaranty, or limiting the Guarantor’s obligation to the Guarantor’s interest in any property (real or personal) pledged to secure repayment of the loan. If a Guaranty is limited, the Authorization will describe the limitation.

The Lender should use a separate Guaranty form for each Guarantor. This will allow greater flexibility in developing a plan for liquidating a loan if that should become necessary in the future. (The Lender may need to sue Guarantors in different states or attempt to collect from one Guarantor after another Guarantor’s liability has been discharged in bankruptcy.)

In the Information Grid at the top of the Guaranty, Lenders must insert information as follows:

- SBA Loan Number and SBA Loan Name: same as stated in the Authorization
- Guarantor: name of Guarantor for this Guaranty; name must match signature block
- Borrower:
 1. Insert ALL Borrower names
 2. No DBAs
- Date: the date this Guaranty will be signed
- Note Amount: principal amount, numbers only

Remember to check the Collateral section of the Authorization for any state-specific conditions that Lender may need to include on the Guaranty form. Collateral securing the Guaranty must not be listed on the Guaranty form.

Settlement Sheet, SBA Form 1050

The Lender is responsible for disbursing loan proceeds strictly in accordance with the requirements of the Authorization; failure of a Lender to do so is a leading cause for SBA to deny its liability under the SBA loan guaranty.

Except for all Express loans, the Lender must document loan disbursements on SBA Form 1050, Settlement Sheet. This form is signed by both the Lender and the Borrower at the time Lender makes the disbursement and must contain sufficient detail for SBA to determine who received loan proceeds, when the loan proceeds were disbursed and in what amount and, most importantly, how the loan proceeds were used.

The Lender must obtain evidence, such as cancelled checks or paid receipts, to ensure that the Borrower used loan proceeds for purposes stated in the Authorization. The Form 1050 also requires Lenders to disburse loan proceeds using joint payee checks when possible.

The Lender must retain the signed SBA Form 1050, Settlement Sheets, as well as all other documents that support the Borrower's use of loan proceeds. If the Lender subsequently requests that SBA purchase the guaranteed portion of the loan, it must submit complete documentation that loan proceeds were used as authorized.

Compensation Agreement, SBA Form 159

An SBA Form 159 must be completed for every representative that the Borrower engages to assist it in obtaining financial assistance. This requirement covers every person (or company) that charges the Borrower in connection with its application, especially loan packagers. If a Borrower employs the services of both an attorney and an accountant, each of them must complete a separate Form 159. Any Agent paid directly by the Lender and not by the Borrower (either directly or indirectly) does not need to complete a Form 159.

The fees paid must bear a reasonable relationship to the services actually performed and be reasonable in the market where Borrower is located. Therefore, contingency fees, where the person providing the assistance is paid only if the Borrower obtains assistance, are not permitted. The fee must relate to the services (and, therefore, the time spent). Therefore, fees that are based upon a percentage of the loan amount sought are not generally approved.

If the fee charged exceeds \$1,000, the representative must provide additional documentation. This includes all of the following: each date a service was rendered, a description of the service, the time spent on that date, and the cost accrued on that date. A bill, for example, that says simply a total of \$x is owed "For Services Rendered" is not adequate.

SBA Forms 722 and 793

These two required forms must be provided to the Borrower in connection with every loan closed. The SBA Form 722 is an “Equal Opportunity Poster” and SBA Form 793 is a “Notice to New Borrowers.”

The poster notifies the Borrower’s employees as well as the public that they have the right under federal law not to be discriminated against. Therefore, federal law requires the Borrower to display this poster “where it is clearly visible to employees, applicants for employment, and the public.”

Form 793 explains to Borrowers what actions they should take to ensure that they are complying with the requirements of SBA regulations and federal law on the subject of non-discrimination. SBA regulations permit the agency to examine the Borrower’s employment, payroll, and related records at any time to confirm that they are complying with federal law. The form also contains a proposal for a “Model Policy Statement” and other suggestions to help the Borrower comply with federal law.

Optional SBA Forms

SBA has kept the number of SBA standard loan closing forms that a Lender must use to a minimum, to allow the Lender maximum flexibility to close its loans efficiently and economically. SBA does, however, offer a number of standard forms that a Lender may use in its own discretion, if the Lender, or its counsel, determines that such forms are legally sufficient under applicable state law. These forms include:

- SBA Form 155, Standby Creditor’s Agreement (Used to restrict the Borrower’s payments to other creditors)
- SBA Form 160, Resolution of Board of Directors (Used to document that a corporate Borrower has authorized the corporation to enter into the loan obligation and authorized certain corporate officers to execute the documents necessary to bind the corporation to the obligation.)
- SBA Form 160A Certificate as to Partners (Used for same purpose as SBA Form 160, but for a partnership Borrower.)

Standby Creditor’s Agreement, SBA Form 155

Frequently, Lenders will want to restrict the ability of the Borrower to pay its other creditors while the 7(a) loan remains outstanding to conserve cash flow. In these instances, the Lender may use SBA Form 155, Standby Creditor’s Agreement to exert control over the Borrower’s ability to pay its other creditors. When using SBA Form 155, the Lender must remember five key points:

- The “Standby Borrower” is the SBA Borrower and the “Standby Creditor” is the Borrower’s other creditor, not the Lender.

- The form contains a menu of choices, which allows Lender to select the appropriate restriction on the Borrower's ability to pay its other creditor(s).
- In order to be enforceable, the Standby Creditor must sign and date the form.
- The Lender's right to stop the Standby Creditor from accepting or retaining payments made by the Borrower is predicated in most cases by the requirement that the Lender separately notify the Standby Creditor to stop accepting payments.
- SBA Form 155 will not subordinate any security interest held by the Standby Creditor in the same collateral pledged to secure repayment of the SBA loan. This must be accomplished with a separate Subordination Agreement.

CHAPTER 3

FACT SHEETS

This chapter provides the Lender with individual fact sheets on the various delivery methods of 7(a) loan processing, closing and servicing. In addition, there is a fact sheet on another SBA loan program specifically designed to finance long-term, fixed assets known as the 504 Program. Although the lender does not receive an SBA guaranty on its participation (generally 50% of the project financing) in this program, the lender receives a senior lien on the project assets with a 100% SBA guaranteed fixed-rate debenture secured by a subordinate lien on the project assets financing approximately 40% of the project costs.

PLP PROGRAM FACT SHEET

SBA's Preferred Lenders Program (PLP) was created in 1984 as a means to delegate much of the Agency's decision making authority regarding loan approval, loan servicing and liquidation activity to lenders who have demonstrated through their SBA-guaranteed portfolios a thorough knowledge of SBA's loan-making and loan servicing requirements.

SOP 50-10(4), subpart D, chapter 3 describes the PLP program including how to become a PLP lender, how a PLP lender expands its PLP area, and the requirements for loan processing under the PLP authority. SOP 5050 4, chapter 6, ¶ 5 covers PLP loan servicing requirements. SOP 5051 2, chapter 10, ¶ 5 covers the PLP liquidation process. All SOPs are available at www.sba.gov/banking.

Lender Eligibility:

Current SBA participants who meet SBA's criteria for being a PLP Lender may apply through their local SBA office. The basic factors SBA will consider are whether or not the lender:

1. Has demonstrated the required ability to process, close, service and liquidate loans;
2. Has demonstrated the ability to develop and analyze complete loan packages; and
3. Has a satisfactory SBA loan portfolio performance history with SBA.

PLP Loan Processing:

The PLP loan approval process is expedited because:

- SBA grants unilateral authority to the PLP lender to make the credit decision.
- For an eligibility determination, SBA only requires a completed checklist from the PLP lender.
- Loans are processed through a centralized processing center.

These procedures typically result in a one-day turnaround time between loan approval request submission by the PLP lender to SBA and SBA's decision. The target time for a standard 7(a) loan between submission and the SBA decision is 13 business days.

Centralized SBA Processing. SBA has centralized the processing of all requests for guaranty using PLP procedures at the Agency PLP Loan Processing Center in Sacramento. The PLP loan applications still must complete all the requested forms and exhibits. However, only a summary of the borrower's information and an eligibility checklist are submitted to SBA. When the PLP lender believes that a loan meets SBA's eligibility criteria and is creditworthy, the lender sends the Center:

1. A copy of the front page of SBA Form 4 which includes the borrower information;
2. A copy of the front page of SBA Form 4-I; and
3. Any forms or checklists required by the Center (to provide evidence of eligibility and required data inputs to generate a loan number).

Lenders submit their applications for SBA guaranty to the PLP Processing Center in Sacramento, California. The address is

PLP Processing Center,
U.S. Federal Courthouse,
501 I Street, Suite 12,
Sacramento, CA 95814;
Telephone 916/930-2410
Fax 906/930-2180.

Business Types Not Eligible For PLP Processing

Certain types of businesses are not eligible to be processed under PLP procedures due to additional requirements for compliance with federal laws and regulations. Some of these are agricultural and farm businesses; fishing and shore operations (including commercial fishing activities and the construction of new fishing vessels; medical facilities (including residential care facilities); and applicants doing business in foreign countries.

Loan Programs Not Eligible for PLP Processing

There are certain types of SBA loans that can not be processed as a PLP loan: These include 7(a) Combination Financing if the PLP lender is making both the commercial loan and the 7(a) loan; Qualified Employee Trusts loans; CAPLines loans; revolving credits except under the Export Working Capital program (EWCP) and then only if the lender has special authority from SBA to make PLP EWCP loans; microloan demonstration loans; third-party loans associated with 504 loans; and any pilot program unless SBA authorizes use of PLP for the pilot. Additional restrictions are found in SOP 50-10(4), subpart D, chapter 3, para. 7.

Post Approval Loan Administration A PLP lender is permitted by SBA to service and liquidate all SBA loans in its portfolio with the same PLP authority. There is no differentiation between loans processed as PLP loans and loans processed as non-PLP loans. In addition, the PLP lender is required to service all SBA-guaranteed loans in its portfolio in the same manner as it services its non-guaranteed loans. The lender's policies and procedures used for loan servicing must be based on prudent and responsible lending practices

The PLP lender may take any necessary servicing or liquidation action consistent with its unilateral authority (as described in SOP 50 50 4, chapters 4 and 6 and SOP 50-51) and prudent lending/credit practices. Prohibited actions include: 1) taking any action that confers a preference on the lender; 2) accepting a compromise settlement without prior written SBA consent; 3) selling or pledging more than 90% of a PLP loan; and (4) handling non-routine litigation or litigation with costs that exceed \$5,000.

LOW DOC FACT SHEET

SBA's Low Documentation Loan Program (LowDoc) Program Guide and all LowDoc forms can be accessed at www.sba.gov/banking/enhance.html#sbalowdoc

LowDoc is a streamlined method by which the Agency provides its guaranty to eligible lenders on loan applications from eligible small businesses that are for \$150,000 or less. The streamlining in this program involves:

- (1) Reduced paperwork for both the lender and applicant once the lender decides to apply for a guaranty on its proposed loan;
- (2) A quicker response by SBA on its decision to guaranty; and
- (3) Alternative post approval responsibilities from standard practices for the lender.

LowDoc relies on the character and credit history of the borrower and the experience and judgment of the lender. The lender is expected to perform credit analysis on LowDoc loans in a manner consistent with prudent lending practices and to summarize that analysis in its request to SBA for a loan guaranty.

Participation in the LowDoc Program is open to existing PLP and CLP lenders, plus other lenders who are experienced in making small business loans of \$150,000 or less, including those which are not currently SBA lenders. Non-PLP/non-CLP lenders who want to become LowDoc lenders must have executed a Loan Guaranty Agreement (SBA Form 750) and be experienced in making small business loans of \$150,000 and less. In accordance with 13 CFR Part 120.410, a lender must have at least 20 qualifying loans outstanding that were initially approved in an amount of \$150,000 or less. Qualifying loans are those that are categorized as commercial, industrial, or commercial real estate loans as identified on Call Reports. Lenders will certify to this fact by signing the LowDoc Application Form.

The maximum amount for a LowDoc loan to any one small business, plus its affiliates, including the balance of any other outstanding SBA debt, except disaster assistance loans, is \$150,000. A business can have more than one outstanding LowDoc loan so long as its total outstanding SBA guaranteed debt of all loans, regardless of the guaranteed portion, does not exceed \$150,000.

To eliminate the need to deal with numerous and varied size standards for different industries, LowDoc has established its own alternative size standard. With a few, specific exceptions, an applicant (including all affiliates) must have annual sales averaged over the preceding 3 fiscal years of \$5.0 million per year or less **and** employ 100 or fewer individuals averaged over the previous 12 calendar months from the date of application. Applications that do not meet the special size standards for LowDoc but do meet regular 7(a) size standards must be processed under procedures other than LowDoc.

In addition, LowDoc loans are **not** allowed under the following SBA programs: Export Working Capital Program, International Trade, CapLines, Defense Loan and Technical Assistance (DELTA), and Pollution Control.

Lenders are to analyze and document LowDoc loans in a manner consistent with prudent lending practices. Instead of the traditional in-depth analysis of a 7(a) application, SBA reviews the information submitted by lenders on LowDoc applications, and, if applicable, the lender's credit analysis and the applicant's financial statements. However, the lender is expected to perform the same level of analysis as it does for similar non-SBA loan requests and consistent with prudent lending practices.

In order to maintain the program's credit quality and streamlined application processes, complicated applications requiring a great amount of explanation or marginal applications which need an in-depth analysis should be submitted under regular 7(a) procedures.

The maximum SBA guaranty of LowDoc loans is 85 percent.

Lenders will submit applications of an SBA guaranty to one of two LowDoc Processing Centers (LDPC), depending on the location of the small business concern being financed. If the business is located in SBA Region I, II, III, IV, or V, the application will be submitted to the Hazard LDPC, 262 Black Gold Boulevard, Hazard, KY 41701, telephone 606/436-0801; fax 606/436-2600. If it is in SBA Region VI, VII, VIII, IX or X, the application will be submitted to the Sacramento LDPC, U.S. Federal Courthouse, 501 I Street, Suite 12-200, Sacramento, CA 95814; telephone 916/930-2410; fax 906/930-2180.

Lender submits only a one-page LowDoc Application Form. Other documents should only be submitted upon request by SBA. Lenders can either fax or mail the application package to the LDPC. SBA Form 4-L, Application for LowDoc Loan, including complete instructions for the applicant and lender and other LowDoc related information, can be found at www.sba.gov/banking/enhance.html#sbalowdoc.

The lender must close LowDoc loans in accordance with the terms and conditions specified in the Authorization as well as according to standard 7(a) procedures.

SBAEXPRESS FACT SHEET

The SBAExpress Program Guide and all SBAExpress forms can be accessed at <http://www.sba.gov/banking/enhance.html#sbaexpress>.

SBAExpress, formerly FA\$TRAK, was established as a pilot program in 1995 and has been extended as a pilot until September 30, 2005.

The SBAExpress program, which also includes the subprogram Export Express, leverages private sector resources by transferring additional authority and autonomy to selected SBA lenders. The program reduces the number of government mandated forms and procedures and streamlines the processing and reduces the cost of smaller, less complex SBA loans. The program allows lenders to utilize, to the maximum extent possible, their respective loan analyses, procedures, and documentation. Lenders can use their own application forms, internal credit memoranda, notes, collateral documents, servicing documentation, and liquidation documentation. However, in using their documents and procedures, lenders must follow their established and proven internal credit review and analysis procedures used for their non-SBA guaranteed commercial loans. In return for the expanded authority and autonomy provided by the program, lenders agree to accept a maximum SBA guaranty of 50%.

Centralized SBA processing. To further reduce program costs, and to ensure program consistency, the current processing of SBAExpress loan applications has been centralized in SBA's loan processing center in Sacramento while loan purchases have been centralized in SBA's Fresno and Little Rock Commercial Loan Servicing Centers. The Sacramento Center reviews the application for completeness and issues an SBA loan number, generally within 24 hours.

Lender eligibility. Current 7(a) lenders who meet the SBAExpress program's minimum SBA loan volume requirements as well as other criteria are eligible for the program. Other lenders who currently are not 7(a) lenders may also be eligible if they meet SBA's lender requirements as set forth in subpart D of SOP 50-10(4) and become an approved SBA lender before participating in SBAExpress. These lenders must continue to meet several performance criteria including acceptable currency in its SBA portfolio, timely 1502 reporting, etc.

Loan eligibility. SBA business loan eligibility, policy, and procedures apply to SBAExpress loans, and the SBAExpress lender must apply all SBA business loan requirements, including those in the Small Business Act, 13 CFR Parts 120 and 121, and SBA Standard Operating Procedures (SOPs 50 10(4), 50 50 4, and 50 51 2), unless specifically identified as inapplicable in the SBAExpress Guide. Also, due to their inherent complexity or other issues, certain types of loans, loan programs, and businesses are not eligible for SBAExpress. Qualified lenders may be authorized to make eligibility determinations.

Credit analysis. The *SBAExpress* credit analysis and credit decision processes are delegated to the lender. However, the lender is required to use appropriate and generally accepted credit analysis processes and procedures, and these procedures must be consistent with those used for its non-SBA guaranteed commercial loans. Acceptable analytical processes include “credit scoring,” if the lender uses credit scoring for non-SBA guaranteed commercial loans.

Loan amount and guaranty percentage. The maximum loan amount for *SBAExpress* is \$2,000,000. The SBA guaranty on an *SBAExpress* loan may not exceed 50%. The aggregate balance of all *SBAExpress* and *FA\$TRAK* loans to a borrower and its affiliates may not exceed \$2,000,000. The aggregate balance of the SBA guaranteed portions of *SBAExpress* and all other outstanding SBA loans to a borrower and its affiliates may not exceed \$1,500,000.

Revolving Line of Credit Loan term. *SBAExpress* revolving line of credit loans may be offered up to a maximum term of seven years, and maturity extensions may be included at the outset of the loan provided the combined term does not exceed 7 years. In addition, an *SBAExpress* revolver may consist of revolving and maturity extensions of any length, as long as the combined term does not exceed 7 years. An *SBAExpress* revolving loan with a term of less than 7 years may be repeatedly renewed, but only up to a maximum of 7 years from the original date of the note. *SBAExpress* revolving loans may be extended past the initial 7 years only as a result of a workout situation.

Interest rate. For *SBAExpress* loans, a lender may charge up to 4.5 percent over the prime rate for loans over \$50,000 up to \$250,000 and up to 6.5 percent over the prime rate for loans of \$50,000 or less, regardless of the maturity of the loan. For variable rate loans, an *SBAExpress* lender is not required to use the base rate identified in the Federal Register. The amount of interest SBA will pay to a lender following default of an *SBAExpress* loan is capped at the maximum interest rates for the standard 7(a) loan program.

Collateral. Under *SBAExpress*, lenders are not required to take collateral for loans of \$25,000 or less. For *SBAExpress* loans the lender must follow the collateral policies and procedures that it has established and implemented for its non-SBA guaranteed commercial loans, which SBA expects will be commercially reasonable and prudent practices for lenders generally. For *SBAExpress* loans greater than \$150,000, the lender must obtain a lien on sufficient business collateral to, in the lender’s judgment, adequately secure the loan.

Fees. The SBA guaranty and servicing fees are the same for *SBAExpress* as for regular 7(a) loans. The lender may charge the same additional fees for *SBAExpress* loans as it charges for its non-SBA guaranteed commercial loans. However, if the loan is purchased by SBA, the Agency will not purchase any portion of the loan balance that consists of these other fees charged to the borrower.

Disbursement of loan proceeds. *SBAExpress* loan funds may be accessed through a variety of methods consistent with the way the lender normally conducts business for its non-SBA

guaranteed commercial loans, including through a credit card. However, lenders are expected to take reasonable and prudent steps to ensure loan proceeds are consistently and exclusively used for business related purposes.

Secondary market. *SBAExpress* loans may be sold on the secondary market. However, for variable rate loans, the base rate must be the low prime rate as published each business day in a national financial newspaper or SBA's Optional Peg Rate.

Loan application. *SBAExpress* loan application packages must include the forms and information the lender requires so that it can make an informed eligibility and credit decision. The applicant must certify the application as true and complete. With some exceptions, the only documentation required by SBA from the applicant under *SBAExpress* is the SBA Form 1919, "SBAExpress Borrower Information Form," which must be signed and dated by the applicant. The *SBAExpress* lender sends to the Center the "Request for Loan Number" and any forms or checklists required by the Center (to provide evidence of eligibility and required data inputs to generate the loan number).

Application for SBA guaranty. The lender requests an SBA loan number from the Sacramento Processing Center. The Center reviews the request for loan number to check that the lender provided the required information and to see if there are any eligibility issues (or for Delegated Eligibility Lenders, to see if the lender certified that the loan is eligible). This is a quick review of documentation. The loan does not have an SBA guaranty until the Center issues a loan number. The lender completes the *SBAExpress* Loan Authorization without SBA review and signs it on behalf of SBA.

Loan closing, servicing, and liquidation. The *SBAExpress* lender must close, service, and liquidate its *SBAExpress* loans using those practices and procedures that the lender uses for its non-SBA guaranteed commercial loans, but under all circumstances, the practices used for *SBAExpress* loans must be reasonable and prudent commercial lending practices. The *SBAExpress* lender may take any necessary servicing or liquidation action for any *SBAExpress* loan in its portfolio, with certain exceptions described in the Program Guide (for which the lender must obtain SBA's prior written approval). *SBAExpress* lenders must complete the liquidation of all *SBAExpress* loans with a remaining collateral value in excess of \$1,000, including those immediately purchased by SBA. In pursuing liquidation after SBA's purchase, *SBAExpress* lenders must provide SBA with a liquidation status report every 180 days until all recovery is completed. Within 60 days of when the liquidation is finished, the lender must provide the Agency with a liquidation wrap-up report summarizing all recovery activity, collections, and expenses and must forward to SBA its proportionate share of any recovery proceeds not already remitted to the Agency.

Guaranty purchase. Generally, SBA purchases its guaranteed interest after the lender has fully liquidated all collateral and the lender has pursued all avenues of collection. However, upon request of a lender, SBA generally will process the purchase immediately upon lender's request: Export Express loans; loans with a principal balance of \$50,000 or less at the time of the

purchase request; and loans that involve, regardless of the loan balance, bankruptcy, judicial foreclosure, litigation, or other unusual liquidation circumstances likely to extend the liquidation process more than 90 days past the earliest date that the lender could request purchase.

EXPORT *EXPRESS* FACT SHEET

The Export *Express* program is designed to help SBA meet the export financing needs of small businesses too small to be effectively met by existing SBA export loan guaranty programs. It is a subprogram of *SBAExpress* and is therefore subject to the same loan processing, making, closing, servicing, and liquidation requirements as well as the same maturity terms, interest rates, and applicable fees as for other *SBAExpress* loans, with some exceptions described in the *SBAExpress* Program Guide.

An SBA Export *Express* loan must be used to develop or expand the small business's export markets. Proceeds may be used to:

- Finance standby letters of credit used for either bid or performance bonds;
- Finance export development activities such as export marketing and promotional activities, participation in foreign trade shows, translation of product literature for foreign markets, and other activities designed to initiate or expand the applicant's export of its products/services from the U.S.;
- Provide transaction-specific financing for overseas orders;
- Provide revolving lines of credit for export purposes, the term of which must not exceed 7 years. (SBA recognizes that in some instances, as a normal course of business, the borrower may use portions of those revolvers for domestic purposes, but SBA expects that no less than 70 percent of the revolver to be used for export related purposes;
- Provide term loans and other financing to enable small business concerns, including small business export trading companies and small business export management companies, to develop foreign markets; and
- Acquire, construct, renovate, modernize, improve or expand production facilities or equipment to be used in the U.S. in the production of goods or services to be exported from the U.S.

Proceeds may not be used to finance overseas operations, except for the marketing and/or distribution of products/services exported from the U.S. Also, existing SBA guaranteed loans may not be refinanced under SBA Export *Express*.

The maximum SBA guaranty on an SBA Export *Express* loan is the same as that for a regular 7(a) loan, or currently 85% for loans of \$150,000 and under and 75% for loans over \$150,000. , Under the Export *Express* program, the aggregate balance of all *FA\$TRAK*, *SBAExpress*, *CommunityExpress*, and Export *Express* loans to a borrower and its affiliates may not exceed \$250,000.

Recognizing that technical assistance can be crucial to the success of small business exporters, SBA Export *Express* includes a technical assistance component, delivered through the U.S. Export Assistance Centers ("USEACs"). When an SBA Export *Express* loan is approved, the

Sacramento Center will notify the USEAC where the borrower is located. The USEAC representative will contact the borrower to offer appropriate assistance, which may include training offered by the Export Trade Assistance Partnership, SBDC International Trade Center, SCORE, District Export Council, or Export Legal Assistance Network.

COMMUNITY *EXPRESS* FACT SHEET

The Community*Express* Program Guide and all Community*Express* forms can be accessed at <http://www.sba.gov/banking/enhance.html#commexp>.

Community*Express* was established as a pilot program in May 1999 with nine participating lenders, later expanded to include PLP and selected non-PLP lenders. The program will run as a pilot through September 30, 2005.

Community*Express* is a cooperative effort between SBA and the National Community Reinvestment Coalition (NCRC) and its member organizations. Under the pilot program, eligible lenders use streamlined and expedited loan processing and approval procedures to increase lending in certain geographic areas that SBA has designated. Under the Community*Express* pilot program, borrowers must receive pre- and post-loan closing technical and management assistance from local non-profit providers and/or from participating lenders, with that assistance coordinated, arranged, and, when necessary, paid for by Community*Express* lenders.

Community*Express* participants are allowed to use, to the maximum extent possible, their own loan analyses, loan procedures and loan documentation. This includes their own application forms, internal credit memoranda, notes, collateral documents, servicing documentation and liquidation documentation. However, in using their documents and procedures, participants must continue to follow their established and proven internal credit review and analysis procedures for loans of similar size and type.

Centralized SBA processing. SBA has centralized its processing of Community*Express* loan applications in SBA's loan processing center in Sacramento. SBA's Commercial Loan Servicing Centers in Little Rock or Fresno handle all routine loan servicing and liquidation issues. Fresno handles all loan purchases.

Lender eligibility. In July 2000 SBA expanded the Community*Express* program to include PLP lenders that have at least a 90% currency rate on their SBA 7(a) portfolio for the last 3 fiscal years and to selected non-PLP lenders that meet the eligibility requirements for participating in the SBA*Express* program.

Loan eligibility. SBA business loan eligibility, policy, and procedures generally apply to Community*Express* loans, and the Community*Express* lender must apply all SBA business loan requirements, including those in the Small Business Act, 13 CFR Parts 120 and 121, and SBA Standard Operating Procedures (SOPs 50 10, 50 50 and 50 51) unless specifically waived by the Program Guide. Lenders can use Community*Express* only for regular 7(a) loans. The same types of businesses that are not eligible for PLP and SBA*Express* are not eligible for Community*Express*. Additional restrictions specific to Community*Express* are set forth in the Program Guide.

Credit analysis. The *CommunityExpress* credit analysis and decision is delegated to the lender. However, the lender is required to use appropriate and generally accepted credit analysis processes and procedures, and these procedures must be consistent with those used for similar size and type loans the lender makes without an SBA guaranty. Acceptable analytical processes include “credit scoring” if the lender uses credit scoring for similar size and type non-SBA loans. The credit analysis technique must be documented, must be kept in the loan file, and is subject to SBA review.

Application. *CommunityExpress* loan packages must include the forms and information the lender requires to make an informed eligibility and credit decision as well as documentation of the assessment the lender makes of the applicant’s management and of the management assistance that the applicant will need. Generally, the only form required by SBA from the applicant is the SBA Form 1919CX, *CommunityExpress* Borrower Information Form, which must be signed and dated by the applicant. The Form 1919CX includes the certifications and requirements set forth in SBA Forms 159, 601, 912, 1261 and 1624. This form does not have to be submitted to SBA, nor does it have to be completed prior to requesting a loan number from the Sacramento Loan Processing Center. However, the lender must ensure that this document is properly executed, by all appropriate individuals prior to disbursement. The lender must keep a copy of the completed Form(s) 1919 in the loan file. The lender is responsible for the completeness of all of the required forms and information.

Application for SBA guaranty. The lender sends to the Sacramento processing center its “Request for Loan Number” and any forms or checklists required by the processing center. The processing center performs a quick look at the applicant’s eligibility, but does not perform any credit analysis. If the processing center determines the loan is eligible and funds are available, it will issue an SBA loan number (usually within 36 hours).

Authorization and loan closing. Once SBA issues the loan number, the lender drafts the Authorization without SBA review and signs it on behalf of SBA. The lender closes and disburses the loan as it would close and disburse its conventional loans. The lender does not have to use SBA forms in closing and disbursing the *CommunityExpress* loans. Prior to disbursement, however, the lender does have to ensure certain conditions specific to SBA lending are met.

Maximum guaranty and loan amount. To encourage participating lenders to aggressively address the targeted markets, and to offset some of the additional costs associated with the technical assistance component, SBA’s loan guaranty under the pilot program is the same as under the regular 7(a) program – a maximum of 85% on loans up to \$150,000 and a maximum of 75% on loans over \$150,000. The aggregate balance of all *CommunityExpress*, *SBAExpress* and *Export Express* loans to a borrower and its affiliates is \$250,000.00. The aggregate balance of SBA guaranteed portions of all *CommunityExpress* and other outstanding SBA guaranteed loans to a borrower and its affiliates is \$1,500,000.

Maximum maturity. Maturities on *CommunityExpress* loans are the same as for any other 7(a) loan, except that revolving *CommunityExpress* loans are limited to a maximum maturity of 7 years. The term of a *CommunityExpress* loan may not exceed the period of the SBA guaranty commitment.

Interest rates. *CommunityExpress* loans are subject to the same maximum interest rate as all SBA loans, as published in the Federal Register. For variable rate loans, a *CommunityExpress* lender is not required to use the base rate identified in the Federal Register. It may use the same base rate of interest it uses on its similar non-SBA loans. However, the interest rate throughout the term of the loan may not exceed the maximum allowable SBA interest rate and the loan may be sold on the secondary market only if the base rate is the low prime rate as published each business day in a national financial newspaper or is SBA's Optional Peg Rate.

Collateral. Under *CommunityExpress*, to encourage smaller loans and to facilitate access to smaller lines of credit, lenders are not required to take collateral for loans of \$25,000 or less. For *CommunityExpress* loans greater than \$25,000, the lender may comply either with SBA's general collateral policy that, to the extent that collateral is available, it must be taken to fully secure all loans backed by taxpayer dollars, or with the collateral policies and procedures that the lender has established and implemented for similar size and type loans not guaranteed by the government, which SBA expects will be reasonable and prudent. Lenders may consider the technical assistance the borrower will receive as a collateral enhancement.

Refinancing: Under *CommunityExpress*, a lender may refinance an existing non-SBA guaranteed loan under certain conditions. Existing SBA guaranteed loans may not be refinanced under *CommunityExpress*, unless the transaction is the purchase of an existing business that has an existing SBA loan that is not with the applicant's *CommunityExpress* lender.

Fees. The SBA guaranty and servicing fees are the same for *CommunityExpress* as for regular SBA loans. The lender may charge the same other fees for *CommunityExpress* loans that it charges for its non-SBA loans of similar size and type, but SBA will not purchase any portion of the loan balance that consists of fees charged to the borrower.

Disbursement of loan proceeds. Lenders may disburse *CommunityExpress* loan funds through a variety of methods consistent with the way the lender normally conducts business for similar size and type loans, including through a credit card. However, lenders are expected to take reasonable and prudent steps to ensure loan proceeds are consistently and exclusively used for business related purposes.

Secondary market. *CommunityExpress* loans may be sold on the secondary market, as long as for variable rate loans, the base rate is the low prime rate as published each business day in a national financial newspaper or is SBA's Optional Peg Rate.

Loan servicing and liquidation. Lenders must service and liquidate *CommunityExpress* loans using generally accepted commercial banking standards employed by prudent lenders. In the

case of revolving loans and loan funds accessed by credit cards or some sort of cash advance system, the lender must use appropriate diligence to ensure ongoing disbursements are used exclusively for business related purposes. The lender must liquidate *CommunityExpress* loans unless SBA advises in writing that SBA will liquidate the loan. The lender must take ordinary protective measures when merited and may recover expenses of protection of collateral from the proceeds of the sale of collateral. Certain actions, specified in the Program Guide, require the prior written consent of SBA. Lenders do not have to submit liquidation plans to SBA, although the lender must document any action taken during the liquidation of a loan. SBA will review liquidation actions as part of the general review of a lender's use of the *CommunityExpress* program.

Guaranty purchase. Generally, SBA purchases its guaranty after the lender has fully liquidated all collateral and pursued all collectible obligors, and SBA has reviewed the loan documentation, which must include lender's liquidation wrap-up report with all the information required by SOP 50-51-2 and copies of the collateral documents.

504 LOAN FACT SHEET

Information about the 504 program is available at <http://www.sba.gov/banking/index504.html>.

ELIGIBLE USES OF THE SBA 504 LOAN:

1. For the purchase of existing building and land.
2. For the purchase of land and the construction of a new facility - must be owner occupied.
3. For renovation, additions, and/or leasehold improvements.
4. For site and land improvements related to the project including at least 5% towards sidewalks, curbs, etc.
5. For major pieces of machinery and equipment that has a useful life of up to 10 years or more.
6. For a small percentage of furniture, fixtures, and office-type equipment.
7. For soft costs related to the project - your attorney and accountant, architect, site planner, engineer, etc.
8. For interim closing costs, including interim interest.
9. An allocation of 10% contingency on any construction or renovation line items.
10. Most fees associated with the funding and closing of the 504 loan can be added to the 504 financing amount; however, the 504 loan cannot fund the CDC's Closing Attorney's fee (approximately \$2,500.00).

SBA 504 ELIGIBILITY FACTORS:

1. The business and any affiliates must have a tangible net worth less than \$7 million.
2. The business and any affiliates must have average net profits after tax of less than \$2.5 million in the last two years.
3. There must be one (1) job created or retained for every \$50,000 of SBA 504 funds, *unless project meets one of the following exceptions:*
 - (A) Business District Revitalization
 - (B) Expansion of Exports
 - (C) Expansion of a Minority owned business (51% or more minority ownership)
 - (D) Expansion of a Veteran owned business (51% or more veteran ownership)
 - (E) Expansion of a Woman owned business (51% or more woman ownership)
 - (F) A Rural Development Project
 - (G) Enhanced economic competition (ex: plant re-tooling)
 - (H) Changes necessitated by Federal Budget cutbacks (ex: military)
 - (I) Business is restructuring arising from federally mandated standards or policies (ex: pollution control, OSHA requirements, etc.

STRUCTURE OF THE SBA 504 LOAN:

In most existing business cases, 50% of the project is funded through a local Participating Commercial Lender, 10% of the project comes from the Applicant as equity - can be cash or land/building value, and 40% of the project is funded by the CDC by using the SBA 504 Loan Program. For new businesses, 2 years old or less, 15% equity is required. For special purpose properties, 15% equity is required. For a new business and a special purpose property, 20% equity is required. In all cases, CDC's portion is reduced when equity is increased.

- * On Real Estate Loans - the 504 loan can have a term of 20 years and the rate is FIXED at funding (usually 1 - 2 points below conventional rates in lender's market area).
- * On Machinery and Equipment Loans Only - the 504 loan can have a term of 10 years and the rate is FIXED at funding.

SBA FUNDING LIMITS:

BA's 40% + the 504 fees can be up to \$1,000,000, unless the applicant meets one of the exceptions listed above as (A) - (I). In this case the 504 loan can be up to \$1,300,000, including 504 fees. *Note: Lenders can meet their CRA requirements when they utilize the 504 loan program.*

CHAPTER 4 - LOAN SERVICING

LENDER SERVICING RESPONSIBILITIES

Loan servicing is the responsibility of the Lender. Lenders must service all SBA-guaranteed loans using generally accepted commercial lending standards employed by prudent Lenders and comply with SBA policies and procedures concerning loan servicing actions (see Appendix 4-A for specific references to SOP 50 50 4, which governs servicing). Lenders must use the same standards for servicing SBA-guaranteed loans as they would for other loans in their portfolio of similar size and type.

SERVICING REGULAR BUSINESS LOANS

SBA recognizes three classifications of loans in servicing:

Approval Status: Loans in “approval status” are loans that have been approved by SBA but either the funds have not been fully disbursed to the borrower or the guaranty fee has not been paid by the Lender. Modification actions for loans in “Approval” Status are governed by the Standard Operating Procedures (SOP 50 10 4), “Loan Processing,” or by the Supplemental Guide for a specific program such as an *Express* Loan Program. (Note: Express includes *SBAExpress*, *CommunityExpress* and *ExportExpress*.) For those loans approved at an SBA Processing Center (Hazard, KY or Sacramento, CA), the requests for approval or acknowledgement of a Lender’s unilateral action are to be sent to the SBA Commercial Loan Servicing Center (CLSC) that covers the geographic area in which the business is located. For loans approved at the local district office, the modifications while in approval status are to be sent to the local office.

Regular Servicing Status: Loans are transferred to “regular servicing” status after all disbursements have been made and after the guaranty fee has been paid. Servicing actions for loans in “Regular Servicing” status are governed by SBA’s SOP 50 50 4, “Loan Servicing.” Requests for approval or acknowledgement of a Lender’s unilateral servicing action are to be

sent to the CLSC that covers the geographic area in which the business is located (see next section of this chapter).

Workouts : In the event of an adverse situation affecting the borrower's ability to repay the loan, all Lenders are required to initiate an effort to determine if the loan can be repaid through an alternative repayment approach. Servicing actions for loans in a workout situation are initiated while the loan is in "Regular Servicing" status and are governed by SBA's SOP 50 50 4. The requests for approval or acknowledgement of a Lender's unilateral servicing action are to be sent to the CLSC that covers the geographic area in which the business is located.

LOAN SERVICING CENTERS

SBA loan servicing is conducted at two centralized loan servicing centers specializing in commercial loans.

SBA CLSC East
2120 Riverfront Dr., Ste 100
Little Rock, AR 72202

(501) 324-5871, x303
lisc.servicing@sba.gov

SBA CLSC West
2719 N. Air Fresno Dr., Ste 107
Fresno, CA 93727

(559) 487-5650
fsc.servicing@sba.gov

The Little Rock CLSC serves borrowers located in the states encompassed by SBA Regions I, II, III, IV and VI (excluding Louisiana and New Mexico), and excluding Puerto Rico & US Virgin Islands.

The Fresno CLSC serves borrowers located in the states encompassed by SBA Regions V, VII, VIII, IX, X and Louisiana & New Mexico, and excluding Alaska & Guam. Lenders in Puerto Rico, US Virgin Islands, Alaska & Guam submit servicing requests to the district office.

LOAN SERVICING REQUEST GUIDELINES

Elements of a servicing request

SOP 50 50 4, Ch. 4

A clear and concise cover letter drawn from information in the Lender's internal credit memorandum generally suffices as the servicing request to SBA. If the cover letter addresses the request and describes the supporting analysis, Lender does not need to submit additional information. SBA may request additional information as individual circumstances require. When submitting requests that involve complex credit or collateral issues, Lender should include its internal credit memorandum with the servicing request but should not submit copies of

financial statements, appraisals or other documents related to collateral unless requested. Lenders are encouraged to submit requests for servicing by e-mail.

In general, servicing requests must address a common set of elements, which allow Lender and SBA to quickly understand the request, the status of the SBA loan(s), the condition of the borrower's business, and other factors important to the decision. The servicing request may require all or a portion of the following items:

- Statement of the proposed action, identification of obligor and a brief description of what makes the request necessary.
- Status of the SBA loan (date and amount funded, current balance and status).
- Summary of the analysis of the business, including analysis of financial statements.
- Summary of prior servicing experience with the borrower, e.g., loan modifications and/or issues pertinent to the request.
- Identification of guarantors/co-makers and a statement as to whether Lender has or will obtain their consent for the action.
- Summary of the impact/benefit of the action on the business.
 - Will the proposed action address the needs or solve the problems of the business?
 - Will the action protect the interest of the Lender and SBA?
- For loans sold in the secondary market, a statement as to whether Lender has given or will give Colson notification of proposed changes to loan terms and whether the secondary market holder has approved the changes.

Additional requirements for actions concerning loan collateral

SOP 50 50 4, Ch. 4, ¶ 6

Lender must protect SBA's interest by maintaining responsible control over collateral items pledged to secure the loan. Lender should fully review the benefits and risks of any loan collateral adjustments.

For actions affecting collateral, Lender must address the following items in addition to those listed above:

- Summary of prior collateral actions approved by the Lender unilaterally and/or by SBA, and

- Summary analysis of collateral before and after the requested change.

Valuation of collateral: Lender is responsible for proper valuation of collateral. The following are general SBA guidelines:

- Appraisals. A recent appraisal prepared by a qualified appraiser must indicate the fair market value of the collateral. If an appraisal is not available, Lender must identify the alternative form of valuation (such as net book value, property tax assessment, internal valuation, etc.).
- Valuation of collateral. Generally, Lender should calculate the net realizable value of collateral by applying the following liquidation percentages to the fair market value (Lender should justify any alternative liquidation values used):

Real Property:

Commercial – RE	75%
Residential - RE	80%
Unimproved Land.	50%

Business Assets (net of depreciation):

Machinery/Equipment.	50%
Furniture/Fixtures	10%
Accounts Receivable/Inventory. . .	20%
Leasehold Improvements	5%

AUTHORITY DELEGATED AND NOT DELEGATED TO LENDERS

To help streamline delivery of its financial services to small businesses, SBA places increased reliance on its private sector lending partners. The SBA encourages its lending partners to utilize “unilateral/delegated authority” (i.e., without prior written consent of SBA) whenever possible. As a result, in the various regulations and SOPs, SBA has delegated to Lenders with certain levels of unilateral authority. Also, under supplemental loan guaranty agreements that SBA signs with Lenders in the PLP and Express loan programs along with the regulations, SOPs, and/or program guides for such programs, SBA has delegated to such Lenders a broad range of authority for actions taken on loans processed under their delegated authority that are in Approval and Regular Servicing status. In SOP 50 50 4, SBA has delegated to Lenders similar authority for loans processed under LowDoc that are in “regular servicing” status. SBA also specifies which actions it has NOT delegated to such Lenders (“non-delegated actions”). For Lenders operating under the standard loan guaranty agreement (SBA Form 750) and not under any supplemental agreement, SBA has granted, limited unilateral authority (in regulations and SOPs) to take certain servicing actions without prior SBA approval when the loan is in Regular Servicing or Liquidation status. All other servicing

actions, for which SBA has not specifically granted unilateral authority, require prior written SBA approval.

SBA expects Lender to perform delegated or unilateral servicing actions without concurrence by or notification to SBA. Lenders must retain documentation regarding the action in its loan file. The exception to the rule is that Lenders must notify the appropriate field office or CLSC in writing when it makes delegated/unilateral changes that will require SBA to make changes to the SBA loans database or accounting records (e.g., interest rate, maturity date, etc.). SBA does not consider changes Lenders make on the 1502 report to be notification to SBA.

It is important for the Lender to recognize that they must NOT exercise “unilateral/delegated authority” indiscriminately. (SOP 50 50 4, Ch. 4, ¶ 12)

- Prudent lending/credit practices must always be used.
- Unilateral actions can be taken only when they:
 - Assist the small business in solving a problem;
 - Assist in its ability to repay the loan;
 - Will not adversely affect the interest of the Lender/SBA; and
 - Are in compliance with all applicable laws and regulations.

Remember that certain terms and conditions were placed in the loan and agreed to by all parties (borrower, Lender/SBA):

- To ensure repayment ability and success of the small business; and
- As a condition to the approval of the loan.

Non-delegated actions for PLP and Express Lenders and for LowDoc loans

13 CFR 120.453, 120.432, and 120.513;

SOP 50 50 4, Ch. 6, ¶ 5(c)(4); 6(2); 7(b)(2);

SOP 70 50 3, Ch. 6

SBA Form 1086 (emergency repurchase from secondary market)

SBA delegates to PLP and Express Lenders, and to other Lenders for LowDoc loans, authority to take all necessary routine “loan servicing” actions without prior SBA approval, **except:**

- Any action that would create a conflict of interest or confer any preference on the Lender in collection or lien position with respect to SBA’s position or the shared SBA/Lender position on the guaranteed loan.
- Compromise with any obligor of the principal loan balance outstanding for less than the full amount due. Lender can adjust accrued interest, if justified, without prior written SBA approval.

- If a loan is delinquent or liquidation is contemplated or underway, prior SBA approval is required to release a guarantor for less than the principal balance owed even if actual demand has not yet been made on the guarantor.
- Title property in the name of the SBA.
- Acquisition of title (in Lender's name or the Agency's) to environmentally impaired property (property which exceeds the minimum action levels established by relevant regulatory agencies).
- Transfer of a loan to another Lender.
- Sell or pledge more than 90% of a loan.
- Increase the loan amount or change the percentage of the SBA guaranty.
- Make an emergency repurchase from the secondary market (*See* SBA Form 1086).
- Handle non-routine litigation or litigation involving legal costs exceeding \$5,000.

Unilateral authority for all other Lenders

*13 CFR 120.10 ("Preference") and 120.513 (actions requiring SBA prior consent);
SOP 50 50 4, Ch. 4, ¶ 10 and 13*

All other Lenders have limited unilateral authority to make certain adjustments in the terms and conditions of a loan if SBA does not consider the action to be "substantial" and the action does not confer preference on the Lender. "Preference" would include but not be limited to a release or subordination of collateral to secure another loan made to the borrower by the same Lender.

Certain actions require the loan to be seasoned for the Lender to be able to exercise their unilateral authority. The term "seasoned" loan applies to a borrower's loan that has demonstrated excellent repayment history over a period of time. For this reason, servicing requirements should generally be less stringent for "seasoned" loans. However, the Lender must exercise care to avoid abuse of the classification. If the Lender takes an action based on the "seasoned" loan classification, the Lender must document this in the borrower's file.

"Seasoned" loans are those loans which meet the following criteria:

- At least 4 years have elapsed since the loan was funded, or for loans under 7 years, where the original principal balance has been reduced at least 25%.
- The loan has been paid "as agreed" for the past 12 months.
- Collateral is at or near "approval" levels, subject to any approved modifications.
- The financial statements are favorable.
- The loan is satisfactory in all other respects.

The following is a listing of allowable unilateral actions such Lenders may take without SBA's prior consent (subject to the restrictions and requirements in SOP 50 50 4, Chapter 4, paragraph 13). This is not all inclusive, but rather a compilation of the most frequently occurring loan servicing actions:

For any of the actions below to be considered as unilateral, it is important for the Lender to read paragraph 13, in Chapter 4 of SOP 50 50 4. Paragraph 13 identifies the policy and procedure for each of the categories below that must be considered for the action to be considered as unilateral.

- Correct obvious typographical errors in the Authorization.
- Provide pay off figures to the borrower.
- Modify financial statement requirements.
- Deferment of principal and/or interest payments.
- Release of collateral.
- Substitution of collateral.
- Subordination to senior liens.
- Changes to life insurance or hazard insurance requirements.
- Adjustments to the installment amount.
- Make loans to the borrower that do not affect the collateral.
- Approve a borrower's change in form of organization (assumption).
- Adjustments to management covenants.
- Accept prepayments.

SERVICING CONCERNS

Initial Interest Rate on Variable Rate Loans (*13 CFR 120.214(a)*, *SOP 50 10(4)*, *Subpart B*, *Chapter 1*, ¶10.a.): Every 7(a) Loan Authorization ("Authorization") establishes the initial interest rate. SBA establishes the initial interest rate at the time it receives the application from the Lender. It is based on the prime rate in effect at that time. Once that rate is established, Lender cannot change it prior to closing regardless of the prime rate in effect. Lender **MUST**

close the loan at the initial interest rate stated in the Authorization. After the initial disbursement, the Lender may change the interest rate on the first calendar day of the month following the date of the initial disbursement, providing this day coincides with the first day of a month designated as an adjustment month (e.g., monthly, quarterly, etc.). All other rate changes MUST be made on the first calendar day of the adjustment interval as stated in the Note (e.g., monthly, quarterly, etc.) following the rate change as reported in the Wall Street Journal.

Interest Rate Basis (*13 CFR 120.214(c), SOP 50 10(4), Subpart B, Ch. 1, ¶ 10.c.*): Lender must establish an interest rate basis before the date of first disbursement and must disclose it on the first SBA Form 1050, Settlement Sheet. SBA policy permits 30/360 (every month is treated as if it has 30 days regardless of the number of days in that month), actual/360 (not permitted for secondary market loans) or actual/365.

Reamortization of Payments: When the prime rate changes and Lender makes a change in the interest rate on a variable rate loan, Lender may reamortize the loan balance for the remaining number of months on the Note. The Lender must notify the Borrower, in writing, of the new payment amount. This will prevent the possibility of a balloon payment at maturity (SBA policy does not permit balloon payments).

Payment Application: For loans in “Regular Servicing” status, Lender MUST apply payments first to interest, up to the date it receives payment; then, the balance (if any) to principal. This is true of all SBA Notes regardless of the payment type (e.g., principal and interest, principal + interest, etc.).

SERVICE CHARGES / FEES

Cancellation of SBA Guaranty for Non-Payment of the Guaranty Fee (*13 CFR 120.524(7), SOP 50 10(4), Subpart B, Ch. 1, ¶ 15.f.*): SBA will automatically cancel its guaranty if Lender does not pay the guaranty fee as required. The Lender must pay the fee within 90 days of loan approval – even if the Lender has not closed the loan with the borrower.

On-going Servicing Fee (*13 CFR 120.220(f)(1&2), SOP 50 50 4, Ch. 3, ¶ 7.*): Lenders are required to pay SBA ½ of 1% of the outstanding (guaranteed portion) of the principal balance on all loans approved after October 12, 1995 through September 30, 2002. The fee was reduced to ¼ of 1% effective October 1, 2002 for loans approved through September 30, 2004. The fee is paid monthly only when Lender has collected interest from the Borrower during that month. Lender CANNOT charge this fee to the Borrower.

Late Payment Fee (*13 CFR 120.221(d), SOP 50 50 4, Ch. 3, ¶ 8.a.*): Lenders may charge a late payment fee not to exceed 5% of the regular loan payment if Lender receives a payment more than 10 days after its due date. The late fee is optional and may be less than 5%. It is the Lender's responsibility to collect the late fee in addition to the regularly scheduled payment. The

late fee is the property of the Lender and does not have to be shared with the investor if the Lender has sold the loan in the secondary market. Lender **MUST NOT** add late fees to the principal balance of the loan under any circumstances. Lender must not add the fees to the transcript of account submitted to SBA when Lender requests SBA's purchase of the guaranty nor can Lender deduct them from liquidation proceeds. SBA will not be responsible for paying late fees at any time under any circumstances. If SBA purchases a loan guaranty, SBA will permit the Lender to collect late charges from the borrower which were owed at the time of purchase, but only after SBA has been paid in full.

Out-Of-Pocket Expenses (*13 CFR 120.221(c), SOP 50 50 4, Ch. 3, ¶ 8.a.*): The Lender may collect from the Borrower necessary out-of-pocket expenses such as filing or recording fees for renewing security interests.

Assumption Fee: The Lender may charge an assumption fee consistent with the Lender's assumption fee on its non-SBA guaranteed loans but must not exceed 1 percent of the total outstanding principal balance of the loan being assumed. This fee may be paid by the seller or the assumptor.

Lender Prepayment Fees (*13 CFR 120.221(e), SOP 50 50 4, Ch. 3, ¶ 8.a.*): A Lender may not charge a *penalty* for full or partial prepayment of a loan.

However, as stated in the Note, the borrower may prepay. Borrower may prepay 20% or less of the unpaid principal balance at any time without notice. If borrower prepays more than 20% and the loan has been sold on the secondary market, borrower must:

- a. Give Lender written notice;
- b. Pay all accrued interest; and
- c. If the prepayment is received less than 21 days from the date Lender receives the notice, pay an amount equal to 21 days' interest from the date Lender receives the notice, less any interest accrued during the 21 days and paid under subparagraph b., above.

If Borrower does not prepay within 30 days from the date Lender receives the notice, Borrower must give Lender a new notice.

Subsidy Recoupment Fee (*13 CFR 120.223*):

For all 7(a) loans where the applications were received by the Lender ON, OR AFTER, December 22, 2000, a new prepayment charge, paid by the borrower to SBA ("subsidy recoupment fee"), has been added for those loans that meet certain criteria. Refer to 13 CFR 120.223 to determine when a loan meets the criteria for this fee. For a prepayment to be determined to be involuntary and therefore not eligible for the fee, the Lender must submit a request to the SBA office servicing the portfolio, which is required to obtain a decision from the Associate Administrator for Financial Assistance (AA/FA) or designee.

Lenders are instructed to report and remit all prepayments along with prepayment fees within 2 business days of receipt to Colson Services Corp.'s Section 7(a) Loan Payoff Department.

Regardless of the secondary market status of the loans, Lenders must report the prepayment and the prepayment fee on SBA Form 1502. Please indicate below the "SBA GP Number" that the subject 1502 remittance is for repayment and prepayment fee. Prepayment fee amount should be reported on the "Remittance Penalty" section of the 1502. The "prepayment amount" does not include accrued interest. It refers only to the principal amount being prepaid. Further information about 1502 reporting can be found at the end of this Loan Servicing chapter.

Servicing Fees on Purchased Loans: If a Lender continues to service a loan after purchase by SBA, the Lender may deduct a service fee on all regular payments collected. Within fifteen days of receipt by the Lender, SBA's share of the payments must be remitted to SBA, Denver, CO 80259-0001 using SBA Form 172. Instructions for computing the service fee are included on SBA Form 172. The Lender must compute the fee based on SBA's participation in the loan and the number of days of interest collected. However, a Lender must NOT collect a servicing fee from principal received (i.e., payments from liquidation proceeds).

COLSON 1502 REPORT

SBA Form 1502 is used by Lenders each month to report 7(a) loan balances, payments, the ongoing servicing fees and status information. This form is mandatory for all Lenders who have SBA guaranteed loans outstanding in their portfolios. Colson Services Corp. (Colson), SBA's Fiscal Transfer Agent ("FTA"), has been designated as the collection agent for guaranty loan balances, status information, payments related to secondary market loans, as well as the ongoing servicing fees.

Colson does not identify the loans for a Lender to report on each month. It is the Lender's responsibility to generate the SBA Form 1502, identify the loans, indicate their status correctly, and forward it to Colson, together with all remittances, by the third calendar day of each month (or the next business day if the third calendar day is not a business day). The form may be in a hard-copy format. However, use of electronic media is strongly encouraged. Funds may also be remitted by wire transfer.

Lenders can use Colson's 1502 template, which is in Excel and Lotus spreadsheet formats. Lenders may remit the 1502 information to Colson on a diskette or via e-mail. The template can be downloaded, at no charge, by accessing the Colson website at www.colsonservices.com (select "Program Forms & Resources") or by calling Colson at 877-245-6159.

Complete the report very carefully. Please double check the status codes entered on the form.

Only report loans as “paid in full” when such loans actually have been paid in full. Do not report the following as paid in full:

- A loan that is being transferred to another Lender; use the status for transfer of the loan.
- A revolving loan with a balance that is paid to zero but which the Lender expects the borrower to continue to use as a revolver in the future; show the loan with a zero balance.

Any time a loan is mistakenly reported as paid in full, it is automatically deleted from SBA’s computer system, the SBA guaranty is cancelled, and the loan file is sent to the Federal Records Center. A Lender can request reinstatement of the guaranty, however, if an adverse circumstance occurs while the guaranty is not in effect, SBA will likely not approve reinstatement and the Lender will have no guaranty for the loan.

Colson’s website (www.colsonservices.com) contains all the information Lenders need to know about 1502 reporting. It includes field descriptions, FAQs, template instructions, fee calculator, Online User Guide, and much more. Lender also can contact Colson Customer Service at 877-245-6159.

CHAPTER 5 - LIQUIDATION AND LITIGATION

This chapter emphasizes SBA's policy that Lenders **MUST** service and liquidate all loans and summarizes SBA policy and procedures relating to lender liquidation.

Appendix 5-A to this Guide is a quick reference guide to SOP 50 51 2, which governs liquidation activities, and to SOP 50 50 4, which governs servicing activities.

GENERAL LENDER-SERVICED LIQUIDATION

This section covers general lender liquidation guidelines. Additional guidelines for special programs (LowDoc, SBAExpress, or PLP loans) are covered later in this chapter.

SBA'S POLICY ON LENDER LIQUIDATIONS

SOP 50 51 2A, Chapter 8, ¶ 1

The lender must:

1. Notify the SBA office servicing the loan of any adverse event (i.e., foreclosure or other legal action, bankruptcy, abandonment, dissipation of collateral) when the loan is transferred into liquidation status.
2. Liquidate a loan in a prudent and commercially reasonable manner.
3. Execute SBA Form 152, "Participation Certificate," showing SBA's guaranty percentage of the loan when guaranty purchase is complete (see Guaranty Purchase chapter). This form is necessary to effectively service and liquidate the loan when guaranty purchase has been completed and the lender still holds the documents.
4. Submit a liquidation plan when required by program rules or regulations.
Liquidation Plans are discussed further below.
5. Maximize recovery in the sale of collateral in the minimum amount of time.

EXCEPTIONS TO RULE REQUIRING LENDER'S HANDLING OF LIQUIDATION

SOP 50 51 2A, Ch. 8, ¶ 10

A. Competing Liens

SBA may take over servicing and/or liquidation of the account if: (1) SBA and the Lender have competing liens against any of the Borrower's assets, or (2) the Lender has a non-SBA loan to the same Borrower or its principals.

If either of these circumstances exist, Lender will be allowed to handle the servicing and/or liquidation, but only if:

1. All disputes have been resolved prior to the commencement of recovery actions, and
2. There is a written agreement as to the distribution of funds and expenses expected to be realized.

B. Past Performance

If a lender's liquidation efforts are or previously have been unsatisfactory, SBA may, at its discretion, take over servicing and liquidation of the account. If a lender is deemed to be unable to properly liquidate loans, SBA may terminate its loan guaranty agreement with the lender. Liquidation responsibilities will be assessed during lender reviews.

INSURANCE

SBA considers it to be a commercially reasonable practice for lenders to purchase or maintain hazard insurance on worthwhile collateral after a loan has gone into default, as well as public liability coverage. Lenders may request that SBA share in the premium expense.
SOP 50 51 2A, Ch. 22

WORKOUTS

SBA encourages the lender to consider workouts wherever possible prior to liquidation.

Lender must notify SBA in writing when a lender has reached a workout agreement with the borrower and is removing the loan from liquidation status. If Lender is receiving payments under a confirmed bankruptcy plan, Lender must provide a copy of the plan to SBA. *SOP 50 51 2A, Ch. 5*

SITE VISITS

Site visits to inspect collateral after default are required. Lenders must perform site visits within specified timeframes (discussed below) and conduct a meaningful collateral inspection. Lenders should prepare a comprehensive listing/inventory of collateral at default along with an assessment of the collateral condition based upon the site visit. Lenders can substitute third party inspection reports from inspection or appraisal services firms as long as the costs are reasonable and customary and the services are provided within the timeframes specified below.
SOP 50 51 2A, Ch. 8, ¶ 8

Timeframes for site visits:

1. Within 60 days of an unremedied default in payment; or

2. As soon as possible after default if there are assets of significant value that could be removed or depleted; or
3. Within 15 days of any of the following events (regardless of delinquency status):
 - a. Business shutdown or abandonment
 - b. Foreclosure or other advance action
 - c. Bankruptcy or receivership
 - d. Any reason to believe the collateral is being lost or its value diminished

PRIVATE NEGOTIATED SALES

A. Lenders liquidating SBA loans may use private/negotiated sales:

1. If it is their usual practice for similar non-SBA assets
13 CFR 120.540 c (1)
2. If the sales were disclosed in their liquidation plan or subsequent amendments to the plan
3. If the lender meets these two requirements:
 - a. Reviews liens on the property to determine that the property is free and clear of all liens, or the lienholders must cooperate in the sale or transfer of title, and
 - b. Has a current appraisal no older than one year to justify the sales price
SOP 50 51 2A, Ch. 8, ¶17-20

B. Some types of sale require a closer review *SOP 50 51 2A, Ch. 8, ¶ 19*

1. Private UCC sales
2. Sales of a "going" business in its entirety
3. Private sales of collateral may not be made to existing owners without prior written SBA approval
4. Term sales – normally apply to real estate. Special compelling needs must exist for a term sale of personal property.
SOP 50 51 2A, Ch. 7, ¶ 6

LENDER'S HANDLING OF LIQUIDATIONS

Liquidation Plans

Prior to initiating recovery procedures lenders are required to prepare a liquidation plan which contains the information referred to in SBA Form 1979, Liquidation Plan Format. For CLP and

regular 7(a) lenders, if the principal balance of the loan at the time of default is **\$50,000 or more**, the liquidation plan must be submitted to SBA prior to starting liquidation action. If the balance at default is **less than \$50,000**, the plan is to be retained in the lender's files, and submitted to SBA at guaranty purchase. *SOP 50 51 2A, Ch. 8, ¶11.b* Except for loans with under \$50,000 principal balance at time of default, SBA must give its consent to the general liquidation plan at the outset (including anticipated litigation) and whenever significant modifications to the plan are needed. PLP lenders must submit a liquidation plan at the time of guaranty purchase for loans with a principal balance over \$50,000. *SOP 50 51 2A, Ch. 10, ¶5.f* The plan must also include "Risk Management Database Information," which are required by legislation and used by SBA in its risk management database. *SOP 50 51 2A, Ch. 4, ¶8* The Liquidation Plan Form may be found at Appendix 15 and the "Risk Management Database Information" at Appendix 16 of SOP 50 51 2A.

The lender must follow procedures that:

- a. Are consistent with generally accepted practices used by prudent lenders
- b. Are required by SBA's SOP, regulations, and loan documents
- c. Use the same degree of prudence as when liquidating non-SBA loans

For CLP loans only: If SBA does not approve, deny, or modify a request for approval of a liquidation plan within 10 business days after the lender makes the request, the plan will be deemed approved. If SBA does not respond to a lender's request for approval of a routine liquidation activity under a liquidation plan within 5 business days after receiving the request, it will be deemed approved. *SOP 50 51 2A, Ch. 10, ¶4.*

The CLP and regular 7(a) lender must obtain SBA's prior written consent for the following actions:

SOP 50 51 2A, Ch. 8, ¶22.

- 1. Sell collateral or real estate owned (REO) to its associates or members of their households.
- 2. Incur legal expenses if lender anticipates legal expenses for litigation will exceed \$5,000. See litigation section below for more information.
- 3. Engage in any non-routine (contested) litigation. See litigation section below for more information.
- 4. Compromise the principal amount of the debt or release an obligor on the loan
- 5. Sell, assign or transfer the note or related loan instruments
- 6. Make a protective bid. A protective bid is:
 - a. The amount of lender's bid at sale

- b. Established based on the current appraisal and expenses related to the foreclosure sale, and should be no higher than the anticipated selling price of the property, less all projected expenses associated with the foreclosure and care and preservation expenses of the property.
- 7. Accelerate the maturity of the note
- 8. Make or consent to any substantial alteration in the terms of the note or related loan instruments
- 9. Approve any release, substitution, or exchanges of collateral, except where the value released does not exceed 20% of the original loan amount
- 10. Sue upon the note or related loan instruments
- 11. Waive any claim against a borrower, guarantor, standby creditor, or other obligor
- 12. Purchase, pay installments on, or pay in full a prior lien
- 13. When the proposed actions vary from either the lender's or the SBA's usual liquidation procedures. The lender must document the circumstances.

Liquidation proceeds must be applied to the SBA guaranteed loan as follows:

Prior to Purchase: If the lender liquidates prior to guaranty purchase, the lender can recover liquidation-related expenses and up to 120 days of interest from liquidation proceeds, using the interest rate in effect at payment default. All other proceeds received from liquidation must be applied by the lender to the principal balance of the loan. SBA will then purchase only its portion of the principal balance outstanding with no accrued interest at the time of the guaranty purchase. *SOP 50 51 2A, Ch. 8, ¶24*

Note: The amount of a lender's successful bid at a foreclosure sale must be reflected on the transcript as a credit to the principal balance of the loan.

After Purchase: When the SBA guaranty **has** been purchased, the lender must apply the net proceeds first to expenses, then to principal, then to interest, unless directed otherwise by SBA. The lender must remit SBA's share of the net proceeds to the Denver Finance Center (DFC) within 15 days of receipt, together with an SBA Form 172, "Report of Transactions on Loans Serviced by Lenders." The Form 172 must indicate the nature of the remittance (liquidation recovery or payment) and itemize any expenses deducted. There is no lender servicing fee on liquidation recoveries. All lender expenses must be customary and reasonable for the services performed and consistent with local practice. Lender must maintain a transcript of account recording all loan payments, liquidation recoveries, fees and expenses properly chargeable to the

loan. SBA Form 172 is available at www.sba.gov/library/forms.html#lender. Online submission of the form also is available. *SOP 50 51 2A, Ch. 8, ¶24-25*

Quarterly status reports

Lenders must submit quarterly liquidation status reports to SBA on all loans after guaranty purchase. SBA may request additional reports at any time. *SOP 50 51 2A, Ch. 8, ¶11.d*

Charge off of loan balance and the Wrap Up Report

If the loan will not be fully repaid after all worthwhile collateral has been liquidated and no further recoveries are anticipated within a reasonable period of time, a final wrap-up report that documents the actions taken to liquidate the account and the results of those actions must be submitted to SBA. If collateral remains that is not cost effective to liquidate due to lack of value, prior liens, environmental concerns, or other reasons, lenders must provide justification in the wrap up report to abandon the collateral. All liens must remain in place, and any future recoveries from the collateral must be shared with SBA according to the guaranty percentage on the loan. The final wrap-up report format is contained in Appendix 18 of SOP 50 51 2A. *SOP 50 51 2A, Chapter 18.*

Further Recovery on Charged-off Accounts

If it is not cost-effective to pursue remaining obligors or guarantors for recovery, and collection action against the obligors/guarantors is still legally permissible (i.e., no bankruptcy, compromise or other legal relief from the debt), SBA will refer them to Treasury for collection. *SOP 50 51 2A, Ch. 18, ¶12* **Note:** If the lender begins further collection action after Treasury referral, SBA must be advised in writing so the Agency can coordinate with Treasury.

LIQUIDATION OF LOANS IN SPECIAL SBA PROGRAMS

Unless specifically addressed in this section, all procedures and guidelines discussed above under general lender liquidation guidelines apply to these programs.

LOW DOCUMENTATION LOAN PROGRAM (LowDoc)

SOP 50 51 2A, Ch. 10 ¶ 1

Liquidation Plan: Approval by SBA of a LowDoc liquidation plan is not required for the lender to pursue recovery actions, and **submission of the plan does not necessarily constitute approval by the Agency or acceptance of its terms.**

Liquidation Expenses: SBA shares in reasonable and necessary costs incurred by the participant on a pro-rata basis up to SBA's share of total recoveries. SBA may agree to pay more on a case-by-case basis in bankruptcy situations. The lender must absorb any excess costs not agreed to by SBA.

Liquidate Prior to Guaranty Purchase: Lenders must liquidate all business personal property on LowDoc loans prior to requesting guaranty purchase, and indicate how the lender will pursue real estate collateral and other assets.

PREFERRED LENDER PROGRAM (PLP)

SOP 50 51 2A, Ch. 10, ¶5

SBA policy requires PLP lenders to take all routine liquidation actions without prior SBA approval on all loans in the PLP lender's portfolio regardless of program type. A PLP lender in one district will liquidate its loans as a PLP lender in all districts except where its authority to liquidate has been terminated because of problems with these functions.

Liquidation Plans: The plan is submitted to SBA at the time of a lender's request for guaranty purchase on loans with principal balances of more than \$50,000. SBA approval of the plan is not required, and **submission of the plan does not necessarily constitute approval of the plan by SBA or acceptance of its terms.**

Non-Routine Actions Requiring Prior SBA Approval:

1. Any action that would create a conflict of interest or confer a preference on the lender in collection or lien position with respect to SBA's position or the shared SBA/lender position on the guaranteed loan.
2. Compromise with any obligor of the principal loan balance outstanding for less than the full amount due. The lender can compromise accrued interest if justified without prior SBA approval.

NOTE: If a loan is delinquent or liquidation is contemplated or underway, prior SBA approval is required to release a guarantor for less than the principal balance owed even if actual demand has not yet been made on the guarantor.

3. Acquire property in the Agency's name.
4. Acquire title in the Agency's or lender's name to environmentally impaired property.
5. Transfer of a loan to another lender.
6. Non-routine (contested) litigation or routine litigation with costs anticipated to exceed \$5,000. See *Litigation* section below for more information on lender-serviced litigation.

SBAExpress PROGRAM www.sba.gov/banking/exguide.pdf

Lenders participating in *SBAExpress* are not required to submit a liquidation plan to SBA, and may use their own documentation and procedures that they use for liquidation of their own loans of similar type/size. Lenders must submit liquidation status reports every 6 months after guaranty purchase on loans with a principal balance over \$50,000.

LITIGATION

Litigation is any matter pending before a judicial or administrative tribunal.

Generally, lenders handling litigation on SBA-guaranteed loans should litigate SBA loans in the same manner as they do their regular commercial loans so long as it is in accordance with **prudent** lending practices. *SOP 50 51 2A, Ch. 10, and SOP 70 50 3, Ch. 6*

The Litigation Plan

A Litigation Plan must be submitted to SBA for prior approval

1. When litigation is not routine (i.e., is contested), or
2. When the cost of litigation activities is expected to exceed \$5000, or
3. Within 15 days of the date of the commencement of any defensive action involving an SBA-guaranteed loan.

Routine litigation is defined as uncontested litigation such as non-adversary matters in bankruptcy and undisputed foreclosure actions. Routine litigation may be handled without prior SBA approval where there are no other outstanding loans made by the lender to the Borrower or any other conflict of interest, as long as fees do not exceed \$5,000.

Contested litigation is defined as litigation in which the facts or legal issues are in dispute. Contested litigation and any litigation in which the lender has another outstanding loan require prior SBA approval.

The Litigation Plan must include certain specified information. *SOP 70 50 3, Ch. 6, ¶ 47*. A proposed Litigation Plan is included as Appendix 5-B. If a Lender fails to submit a litigation plan when required, reimbursement of fees and costs may be limited to those fees and costs that SBA counsel determines were necessary and reasonable.

Lender Reporting after SBA Approval of the Litigation Plan

1. Copies of **legal invoices** must be sent to SBA **when received**. SBA counsel will review the legal invoices to determine whether :
 - a. The fees are customary and reasonable
 - b. The fees do not exceed those charged the lender for non-SBA litigation
 - c. The services do not include non-legal liquidation services
 - d. Outside counsel does not double-bill for unnecessary work or work that only benefits the lender
 - e. Lender's in-house counsel does not bill for legal work
2. Copies of **substantive pleadings** such as dispositive motions or other pleadings containing substantive legal arguments or statements of policy must be submitted to SBA **prior to filing**.
3. An **amended litigation plan** must be submitted to SBA if a modification is necessary or if the costs exceed projections by 5%.

SBA will not reimburse a lender for:

1. Any legal fees and costs incurred by lender in an action brought by lender against SBA or in defense of an action brought against lender by SBA;
2. Any legal fees and costs incurred by lender in joining SBA in the litigation by way of cross-claim or counterclaim;
3. Any legal fees and costs incurred by lender's outside counsel for performing non-legal liquidation services;
4. Actions which solely benefit lender as determined by SBA counsel;
5. Defense of lender liability cases except where the lender's actions were expressly approved by SBA; or
6. Attorney fees and costs not proposed in a Litigation Plan, unless determined by SBA counsel to be necessary, reasonable, and customary in the locality in question.
7. Fees for legal work done by in-house counsel.

SBA may assume litigation responsibilities when:

1. The Lender has an actual or potential conflict of interest;

2. The cost of Lender's counsel is not cost-effective in terms of potential recovery;
3. There is a risk of adverse precedent to SBA;
4. The litigation presents important policy or legal issues;
5. The special remedies available to SBA would produce a greater recovery.

COMPROMISE OF DEBT

GENERAL SETTLEMENT POLICY

SBA approval is required for all compromises of principal. Lenders are expected to evaluate compromise/settlement offers and prepare for SBA's review a recommendation to either approve or decline. *SOP 50 51 2A, Ch. 17*

Lenders should explore the possibility of a compromise prior to:

1. Initiating litigation for judgment
2. Commencing foreclosure against a personal residence

Any settlement amount must bear a reasonable relationship to the present value of the estimated amount of recovery available through foreclosure (using a forced sale equivalent value) and enforced collection. This value, combined with the earning potential of the debtor, will form the basis for the offer. *SOP 50 51 2A, Ch. 17, ¶8-12.*

a. Forced sale equivalent and enforced collection:

The basis for this value is normally the amount recoverable from the sale of assets within a limited period of time (auction type sale). A consideration should also be made as to the time and expense required to gain control of the assets (foreclosure, eviction) and holding costs.

b. SBA considers the following factors when evaluating a compromise:

- Court costs, filing fees
- Prior liens, taxes, assessments
- Costs of sale (auctioneers, advertising, clean up)
- Possibility of contested litigation, bankruptcy and related expenses

- Time mandated by state redemption periods and the resulting costs involved
- Care and protection expenses pending resale
- Extraordinary expenses of eviction, repair, vandalism
- Discount reflecting the present value of future net recovery

Fraud or Misrepresentation

An Offer in Compromise **cannot** be accepted if there is knowledge of fraud, misrepresentation, or financial dishonesty on the part of the offeror. The settlement of claims involving these issues is reserved for the DOJ.

THE COMPROMISE PACKAGE

A. Offer must be in writing from the obligor with specific terms specified (i.e. cash, note, or a combination thereof)

B. Information needed from offerors: SOP 50 51 2A, ¶7

1. SBA Form 1150, Offer in Compromise

SBA Form 1150 must contain the offer and be signed by each person making the offer. Offers submitted in some other format are acceptable if they make reference to 18 U.S. Code 1001 and use the Code language found on the SBA 1150 and are signed by each person making the offer; and,

2. SBA Form 770, Financial Statement of Debtor

A balance sheet and statement of income and expenses which covers each obligor(s) or guarantor for the most current year. SBA Form 770 or the equivalent must be used. Signed copies of federal income tax filings are acceptable for the income and expense requirement.

C. Information lenders need to submit to SBA:

Lender write up recommending acceptance or decline of the offer, presented in a manner consistent with and containing the information specified in Appendix 27 to SOP 50 51 2, "Recommended Compromise Report Format."

CHAPTER 6 - GUARANTY PURCHASES

SOP 50 51 2A, Ch. 13

REQUESTING THAT SBA HONOR ITS GUARANTY

SBA reviews a lender's request that SBA honor (purchase) the guaranty to determine whether the lender has complied with SBA loan requirements and prudent lending standards so that payment of the guaranty is appropriate. The amount and types of documentation that lender must include in its guaranty purchase package depends on the type of loan, use of proceeds, collateral, and other factors. SBA conducts its review prior to purchasing its guaranty when SBA purchases directly from the lender ("pre-purchase review"), and conducts its review after purchasing its guaranty when SBA purchases directly from the secondary market holder ("post-purchase review"). SBA rarely purchases without a lender demand, but it has regulatory authority to do so in its sole discretion (13 C.F.R. § 120.520).

SBA PURCHASE REQUIREMENTS

In addition to any agreements a lender has signed with SBA, the following are sources of information on SBA requirements for purchases:

- Regulations: 13 C.F.R. §§ 120.120 - 120.124.
- Standard Operating Procedures (SOPs):
 - SOP 50 50 4A, Ch. 9 and 10;
 - SOP 50 51 2A, Ch. 13;
 - SOP 50 50 4A Ch. 6, para. 6.c (LowDoc loans);
 - SOP 50 50 4A Ch. 6, para. 9.f (Export Working Capital Program (EWCP) Loans).
- Notices General:
 - Procedural Notice 5000-898 (Dec. 2003);
 - Policy Notice 5000-831 (October 2002)
- Notices on *SBAExpress*:
 - Information Notice 5000-819 (Sept. 2002);
 - Procedural Notices 5000-813 (July, 2002); 5000-803 (June 2002)
- Forms: Guaranty Purchase Checklist (Appendix 6-B)
- Program Guides: *SBAExpress* Program Guide, Sections (Secs.) 8 and 9.

TIME TO REQUEST PURCHASE

A lender first may request payment on the SBA guaranty for loans made under most SBA loan programs following a 60-day uncured delinquency. However, in all loan programs SBA strongly encourages lenders to fully liquidate the loan prior to requesting purchase.

Special rules for certain loan programs:

- LowDoc Loans (SOP 50 50 4A Ch. 6, Para. 6.c.)
 - A Lender can request purchase when:
 - Lender has liquidated all personal property, except in bankruptcy situations, and
 - Lender has indicated in writing how it will pursue all other sources of recovery.
 - SBA will pay a maximum of 120 days of accrued interest.
 - SBA will share in the reasonable and necessary expenses on a pro-rata basis up to its share of total recoveries.
- SBAExpress loans (SBAExpress Program Guide, Sec. 8)
 - Lender can request purchase when it has fully liquidated all collateral and pursued all avenues of collection. Exceptions:
 - SBA will immediately process the purchase request of all Export Express Loans; and
 - SBA will immediately process the purchase request of any SBAExpress loan that:
 - Has a principal balance of \$50,000 or less at the time of the purchase request, or
 - Involves, regardless of the loan balance, bankruptcy, judicial foreclosure, litigation or other unusual liquidation circumstances likely to extend the liquidation process more than 90 days past the earliest date that the lender could request purchase. (Generally, the earliest date a lender could request SBA to purchase is when there has been an uncured default exceeding 60 days.)
 - When requesting the purchase of an SBAExpress loan with a balance of \$50,000 or less, the lender generally will not be required to substantiate the liquidation of business assets, although the lender must document the liquidation of all business assets in its wrap-up report.
 - SBA will pay up to 120 days of interest.
- EWCP (SOP 50 50 4A, Ch. 6, Para. 9.f). Lenders may make demand as soon as the loan is classified as being in liquidation and 30 days after the earliest uncured payment default, but must not make demand later than 120 days after the earliest uncured payment default (See also SOP 50 51 2A, Ch. 10, Para 3).

HOW AND WHERE TO REQUEST PURCHASE

SBA encourages lenders to submit purchase documentation in a uniform and organized fashion, which may also result in a faster processing time by SBA. SBA recommends that lenders use the Guaranty Purchase Checklist, and place documents in the purchase package in the same order as they are listed in the Checklist (each document is assigned a number on the Checklist, in the left-hand column), with corresponding numeric tabs or hand-written numbers on the front of the document, lower right-hand corner.

Purchase requests, along with all documents required for processing, should be submitted to the office that currently oversees servicing of the loan. If the loan is in regular servicing status in either the SBA Fresno or Little Rock Commercial Loan Service Center, send your request directly to the appropriate center, and the loan file and your purchase request will be sent by that office to the National Guaranty Purchase Center located in Herndon, Virginia. If your loan is in liquidation status and already assigned to the Herndon center, send your guaranty purchase request directly to Herndon and your request will be matched with the loan file and assigned to a loan officer.

Addresses for the Commercial Loan Servicing Centers:

SBA CLSC East
2120 Riverfront Dr., Ste 100
Little Rock, AR 72202

SBA CLSC West
2719 N. Air Fresno Dr., Ste 107
Fresno, CA 93727

(501) 324-5871, x303

(559) 487 – 5650

Address for the National Guaranty Purchase Center:

SBA National Guaranty Purchase Center
1145 Herndon Parkway, Ste. 900
Herndon, VA 20170

(703) 487-9283

- The address to access the purchase center's web page is <http://www.sba.gov/banking/herndon.html>.
- You may e-mail the center at sbapurchase@sba.gov for issues relating to guaranty purchases, or loanresolution@sba.gov for general liquidation issues.
- Questions or concerns may also be faxed to 202-481-4674.

DOCUMENTATION REQUIRED FOR PURCHASE

Streamlined and Standard Purchases: SBA has two types of purchase procedures, depending on the size of the loan balance remaining at the time of lender's purchase request and other factors: streamlined purchase procedures and standard purchase procedures. In all cases, a Lender must submit, at a minimum the following documents (see Guaranty Purchase Checklist):

- (1) Written demand that SBA purchase the guaranty, including,
 - Date of default
 - Interest-paid-to date
 - Interest rate at time of default (see discussion in Standard Purchase Procedures regarding reimbursable interest)

- Next installment due date
- (2) Wire transfer instructions
- (3) Certified transcript of account (SBA Form 1149 or lender's equivalent) signed by the lender (see discussion below for details)
- (4) Copy of signed Authorization and amendments
- (5) Copy of signed Note (must be on SBA Form 147 except *SBAExpress* loans)
- (6) Copy of signed Guaranties (if required by the Authorization) (SBA Form 148)
- (7) Risk management database information
- (8) If the lender has completed liquidation on the account, the lender also must submit:
 - Lender certification that liquidation is complete and that all avenues of recovery have been exhausted
 - Final liquidation wrap-up report
- (9) For LowDoc and PLP Loans, documentation relating to the lender's eligibility determination (see discussion below)

Lender Transcript of Account: SBA requires lenders to submit for all guaranty purchases a Transcript of Account (SBA Form 1149 or lender's equivalent). Directions for completion of SBA Form 1149 are located on SBA's website at www.sba.gov/library/forms.html. While lenders have a variety of automated reporting and tracking systems and so may provide their own transcript as an alternative to the SBA Form 1149, the transcript of account **must** contain these elements:

- SBA loan name and 10 digit loan number.
- Method used for interest computation (360 day or 365 day).
- Date and amount of each disbursement.
- Date and amount of each payment showing principal and interest applications.
- Date to which interest is paid (which should be the same date payment was received).
- Interest rate changes (for variable rate loans).
- Next payment due date (defined as the "default date," at which point the interest rate becomes fixed; no changes to the rate should be reflected thereafter).
- If applicable, amount of Lender's successful bid at foreclosure sale (reflected on the transcript as a credit to the principal balance).

If lender uses its own form of transcript of account, lender must provide the following certification:

"I certify this to be a true copy of transcript of account."

Name

Date

Title

Lender Name

Loan eligibility documentation for PLP-processed and LowDoc loans: For all purchases involving loans processed as PLP, SBAExpress or LowDoc, SBA will review the eligibility of the loan for SBA-guaranteed financing, because SBA does not perform an independent review of eligibility at the time of loan approval. Lender must provide a copy of the eligibility checklist and supporting documentation lender used in its eligibility determination. If a PLP, SBAExpress or LowDoc loan is found to be ineligible, SBA will request that the lender voluntarily release the guaranty (or repay SBA if SBA purchased the loan from the secondary market). Note: a completed eligibility checklist alone will not be sufficient in confirming that the loan was eligible.

Streamlined Purchase: SBA will follow a streamlined purchase procedure, and generally not request additional documentation from the lender, if the following three criteria are met:

- (1) The SBA share of the outstanding principal loan balance is \$10,000 or less; and,
- (2) The loan did **not** experience early default/early loan problems (see below); and,
- (3) There is **no** suspicion of fraud or misrepresentation and **no** indication of a conflict of interest on the part of the borrower or lender.

Early default or early loan problems: SBA will not purchase early default or early loan problem loans using the streamlined purchase procedure. “Early default” means that a default in payment or business failure has occurred either prior to final disbursement of the loan, or within 18 months from the date of final disbursement. A default includes an unremedied failure to make one or more loan payments in accordance with the terms of the Note, as well as events that would place a loan in liquidation (see SOP 50 51 2A, Chapter 4, Paragraph 6). “Early loan problems” arise when either prior to final disbursement or within the first 18 months after final disbursement, a borrower consistently makes late payment (over 60 days late) or partial payments, or funds monthly payments through the sale of collateral, or the lender has deferred two or more consecutive scheduled payments. SBA reviews early default or early loan problem loans with a very high degree of scrutiny, and determines whether any deficiency by the lender in making, servicing, or closing the loan contributed to, or allowed, the early default or early loan problems. For all guaranty purchase reviews involving a PLP-processed loan that has gone into early default or experienced early loan problems, the lender must submit complete copies of its credit memorandum, supporting documentation relied on in its credit analysis, the borrower's application for the loan, and SBA Form 912 (Statement of Personal History) for each principal.

Additional documentation required for standard purchase procedures: If a loan is not eligible for streamlined processing, SBA will notify the lender as to which additional documents it will need for its purchase review by checking the appropriate boxes on the Guaranty Purchase Checklist. However, lenders may be able to expedite SBA’s review through providing the following documents in its initial purchase package, as applicable given the terms of the loan.

- **Site visit report:** Lenders must perform site visits within specified timeframes and prepare a comprehensive and detailed report containing an inventory of assets and an assessment of their condition (see SOP 50 51 2A, Chapter 8, para. 8). Lender must include such site visit reports in its purchase package. If the site visit report indicates that

collateral valued at more than \$5,000 was missing at time of the site visit, a referral to SBA's Office of the Inspector General (IG) is mandatory. A copy of the lender's IG referral should be included in the purchase package. Refer to SOP 50-51-2A, Chapter 24, para. 7.a.(2).

- **Bankruptcy:** If a bankruptcy has been filed and lender has not previously notified SBA, the purchase package should include the bankruptcy schedules, notices, other court filings, and proof of claim filed by the lender. If lender does not submit this information, SBA may not process the purchase request, depending on the type of bankruptcy filing and the date of the filing, because the information may have a significant impact on the determination of SBA's obligation to honor its guaranty.
- **Use of proceeds:** The lender must submit documentation that shows the lender disbursed the loan proceeds in accordance with the Authorization. With the exception of *SBAExpress* loans, the lender must submit copies of the Settlement Sheet (SBA Form 1050) used in disbursing the loan.
- **Deeds of trust/mortgages:** If the Authorization requires real estate collateral to secure the note or a personal guaranty, the lender must include a copy of the deed of trust/mortgage in its purchase package. SBA reviews the deed of trust or mortgage to determine whether it was properly executed and recorded.
- **Title policy:** When real estate is required as collateral, the Authorization generally requires a title policy or report. If required, a copy must be provided in lender's purchase package.
- **Guaranty (SBA Form 148):** Holders of a 20% or more ownership interest in the small business generally must guarantee the loan. SBA Form 148 is a mandatory form and lenders cannot substitute their own form (this also applies to SBA Form 148L, Limited Guaranty).
- **Appraisals:** If an appraisal was required in the Authorization or by SBA policy, lenders are required to submit, at a minimum, the summary section from the beginning of the appraisal that indicates the appraised value and the date of valuation. However, SBA may request a copy of the full appraisal.
- **Environmental issues:** The environmental requirements for processing 7(a) and 504 loans are set forth in Chapter 1 of this Guide. The Authorization will state if any environmental reports were required. If so, the lender must submit, at a minimum, the summary and recommendation pages from any environmental report obtained, or if no report was obtained, an explanation for this omission with citation to the relevant provisions in SOP 50 10 4E.

- **Business asset collateral:**
 - **Security agreement:** If the Authorization required business personal property collateral, the lender must submit a copy of the security agreement with its purchase package. SBA reviews the agreement to determine whether it was properly executed by the appropriate individual or entity.
 - **UCC financing statements and renewals:** Lender must submit evidence of UCC lien filings and renewals, along with necessary lien searches. SBA will determine whether Lender properly perfected its lien and obtained the lien position required by the Authorization. If Lender has sold the collateral, SBA will review the recovery and expenses to assure that the Lender properly handled the liquidation and maximized recovery consistent with its lien position. If Lender did not obtain the proper lien position, SBA will analyze the amount of loss to SBA, if any, resulting from the improper lien position. If lender obtained a lien on the required collateral but did not include a lien search in its purchase package, SBA may proceed with the purchase but notify the lender that SBA will review liquidation of the remaining collateral later, to determine if there was any material loss to SBA if the lender failed to obtain the required lien position.
- **Life insurance:** If the Authorization required life insurance on a principal of the borrower or guarantor, SBA may require documentation pertaining to proper assignments and the continuation of coverage.
- **Flood insurance:** If required by the Authorization, lender should provide either: (a) certification that collateral is not located in designated flood area, or (b) evidence of flood insurance coverage.
- **Hazard insurance:** Lender must submit evidence of hazard insurance coverage and a lender's loss payable clause (for personal property collateral) or mortgagee clause (for real property collateral). If a policy has lapsed, lender should submit copies of the letters sent to borrower and all guarantors notifying them of lapse of coverage and requesting reinstatement.
- **Borrower injection:** If the Authorization requires borrower injection (usually in the form of cash or assets), lender must obtain evidence that the injection was made *prior to first disbursement*.
 - **Cash injection:** The Authorization will state the amount of the required cash injection, and usually the intended use. Satisfactory evidence for a cash injection generally consists of copies of processed checks, bank account statements (showing the borrower's account balances before and after the injection) dated prior to but near loan disbursement, or a signed and dated escrow settlement statement along with a bank statement showing the injection into the business.

Lender must submit credible evidence that the borrower did not use the disbursed loan proceeds to fulfill the cash injection requirement. If a cash equity injection is material to the borrower's operation, the lender must verify and document the existence of the cash injection so that it can reasonably be presumed that the funds will be used for business purposes.

- **Injection using borrowed funds:** The Authorization will set forth the documentation required; generally, there must be a full standby agreement (SBA Form 155 or comparable) providing that the loan for cash injection will not be repaid until the SBA loan is fully paid. If a standby is required, lender should submit a copy of the standby agreement and a copy of the debt instrument. If the lender makes a loan to an individual for purposes of a cash injection (or is aware of a loan made for this purpose), the lender must provide a full standby agreement or demonstrate that the loan can be repaid from a source other than the borrower business, or from reasonable withdrawals of salary from the business.
- **Asset injection:** The Authorization will specify the valuation requirements; appraisals may be required. The dollar amount of assets to be injected is based on the fair market value of the assets at loan inception. SOP 50 10 4, subpart A, chapter 4, paragraph 1(f) (4) requires lenders to carefully determine the value of non-cash assets injected into the business.
- **IRS tax verification:** On loans approved after October 7, 1994, SBA requires IRS tax verification transcripts to be obtained from the IRS using Form 4506, except for start-up businesses. These must be part of the purchase package for all early default/early loan problem loans, and may be required on loans that go into default later if necessary for the purchase review. The IRS verification policy applies regardless of whether it is specifically mentioned in the loan authorization.

Borrower resolutions deleted

- **Collateral lists:** Some Authorizations require that the lender obtain a listing of collateral prior to closing the loan, complete with a description and serial number of the items. The lender should provide a copy of the list with the purchase package.
- **Liquidation and Litigations Plans:** If the lender is requesting purchase prior to conducting liquidation and debt-collection litigation, these plans may need to be included with the purchase request if not already submitted to SBA.

PAYMENT OF INTEREST

(1) If SBA receives a lender's complete purchase package within 120 days of default, then all interest is payable to the date of the purchase payment, including interest during the time SBA is processing the purchase, and also from the interest-paid-to-date until the date of default.

(2) If SBA does not receive lender's complete purchase package within 120 days from the date of default, only 120 days of interest is payable.

(3) If lender has liquidated the loan prior to requesting purchase, lender is allowed to recover up to 120 days of accrued interest from liquidation proceeds.

The rate of interest is the rate in effect on the day that the loan went into default. These interest days should begin with the interest-paid-to date up to 120 days maximum. SBA will then purchase the guaranteed principal balance remaining. Late charges are not covered under SBA's guaranty agreement with a lender and therefore lender cannot recover such fees from liquidation proceeds.

Due to legislative changes, for loans that were approved between September 28, 1996 and September 30, 2000, SBA will pay the lender the rate of interest indicated in 13 C.F.R. § 120.122 less one percent. SOP 50 50 4A, Ch. 9, Para. 8.b. Congress eliminated this requirement for loans approved after September 30, 2000. See SBA Procedural Notice 5000-703 (Dec. 2000).

Lender also should refer to the discussion below of the payment of interest for guaranties that are sold in the Secondary Market and 13 C.F.R. §§ 120.521, 120.522, and SOP 50 50 4A, Ch. 9, Paras.7-8.

PURCHASE FROM THE SECONDARY MARKET

SBA strongly encourages lenders to purchase directly from the secondary market holder those defaulted loans that lenders had sold in the secondary market after loan closing and disbursement. If the lender will not purchase, it must notify SBA in writing, and SBA will immediately purchase the loan and then perform a post-purchase review. If the lender purchases from the secondary market, and subsequently requests an SBA purchase, SBA will perform a standard pre-purchase review.

Documentation for secondary market purchase by SBA

- **Written notice and request for transcripts:** The lender must advise SBA **in writing** that it will not purchase from the secondary market. SBA will then notify both Colson Services Corp. and the lender that SBA will purchase the guaranteed portion. The lender must send any future loan collections to SBA's Denver Finance Center using SBA Form 172.
- **Complete and certified lender's transcript of account:** Within 5 business days of receiving SBA's notice of intent to purchase from the secondary market, the lender must submit to SBA a complete and certified transcript of account. SBA will reconcile the transcripts provided by Colson and the lender. SBA may request the lender's assistance in

the reconciliation process. If a lender's transcript is not received timely, or if SBA cannot complete reconciliation, SBA will use the Colson transcript and proceed with the secondary market purchase.

- **Payment of accrued interest:** SBA must purchase all accrued interest from the interest-paid-to date up to the date of guaranty purchase from the secondary market holder. If there was a delay in purchase caused by the lender, SBA will bill the lender for the excess interest purchased.
- **Post-purchase review:** SBA will conduct a post-purchase review to determine the appropriateness of the guaranty payment. In order to expedite the post-purchase review and minimize documentation requests, SBA recommends that lenders submit a complete guaranty purchase package to SBA using the procedures outlined above for standard purchase reviews. Lender should submit the package either concurrently with the written demand for purchase or shortly thereafter. If a lender fails to provide necessary documentation requested by SBA within 30 calendar days of the request, and fails to provide a satisfactory written explanation as to why it cannot provide the requested information, SBA may consider this to be a material failure to comply with SBA loan requirements and can serve as a basis for SBA to seek recovery from the lender of the amount paid to the secondary market under the guaranty. Similarly, missing documentation can support a partial recovery to the extent that the documentation in question relates to specified collateral or other loan requirements.

DENIALS OF LIABILITY AND "REPAIRS"

SBA's general policy for guaranty purchases is to reach a fair decision based on a thorough review of lender's purchase request and all relevant documentation. If a lender has been deficient in its handling of a loan, the SBA office processing the purchase will attempt to reach an equitable resolution with the lender, which may involve the lender agreeing to a monetary adjustment in the amount of SBA's guaranty (referred to by SBA as a "repair"). However, SBA may consider a denial of its liability under its guaranty or litigation to recover funds SBA already paid under its guaranty to the lender (or secondary market holder) if the lender is not negotiating in good faith, the lender is unwilling to agree to a repair that reflects the harm caused to the SBA, or the lender's actions are sufficiently serious that a repair would be inappropriate.

SBA regulations at 13 CFR §120.524 describe when SBA will be released of liability on a loan guaranty. Lender also should consult the guaranty purchase procedures in SOP 50 50 4A, Chapters 9 and 10, and SOP 50 51 2A, Chapter 13.

Expiration of guaranty after maturity: If the lender fails to request purchase within 120 days after loan maturity, SBA is not legally obligated to purchase the guaranty. 13 C.F.R. § 120.524. Under certain circumstances, SBA may permit reinstatement of the guaranty and extension of the maturity (thereby extending the period during which the lender may request purchase). For example, reinstatement may be appropriate if the lender was actively servicing or liquidating the

account with SBA knowledge or concurrence, and inadvertently failed to timely request purchase or extend the loan maturity.

CHAPTER 7 - LENDER OVERSIGHT

The SBA Office of Lender Oversight (OLO) is responsible for overseeing lenders that participate in the 7(a) and 504 SBA loan guaranty programs. OLO's mission is to support SBA's lending programs through an assessment of the SBA-guarantee risk associated with 7(a) and 504 loans and by monitoring lenders' adherence to applicable legal and regulatory requirements.

OLO identifies and analyzes the risk profile of each lender. OLO also conducts off-site assessment and monitoring of all lenders, and periodic on-site reviews of lenders that represent significant risk to SBA in terms of dollars guaranteed and loan portfolio credit quality.

LOAN AND LENDER MONITORING

OLO's loan and lender monitoring activities include a database of information about SBA's loans and lenders which is used to monitor lender and portfolio performance. Analytical data generated from the loan monitoring system significantly enhances OLO's ability to measure and evaluate the guarantee risk within SBA's small business guaranteed loan portfolio.

OLO's intent is to focus its attention on lenders that, in SBA's judgment, present the highest guarantee risk profiles and to tailor monitoring and reviews to identify and address high risk lending activity.

Lender Risk Assessment Process

OLO evaluates all lenders quarterly on issues related to loan portfolio credit quality, SBA exposure, and other factors. This quarterly assessment is a deciding factor in determining the level of oversight a lender receives. Oversight can range from off-site monitoring to on-site lender reviews on a 12 to 24 month cycle. Utilizing available information, OLO calculates a projected purchase rate for each lender. OLO then ranks lenders based on the percentage of the lender's SBA loan portfolio that presents a guarantee risk to SBA. The lender risk assessment process also may consider a variety of other quantitative data as well as other pertinent information to assess the lender's ability to evaluate, process, close, disburse, service and liquidate its portfolio in a manner that will minimize the guarantee risk to SBA. OLO's risk-based monitoring program consists of two interrelated activities: off-site assessment activities and on-site reviews.

Off-Site Lender Assessment and Monitoring

OLO conducts off-site monitoring based on quarterly assessments of lenders and their loan portfolios. In addition to credit quality assessments, the quarterly analysis also includes performance analysis and peer group comparisons and evaluates loan portfolio performance as it relates to demographic criteria, which may include geography, industry, lender size, and SBA program activity. The off-site assessment allows OLO to identify those lenders whose risk profiles have changed significantly since the last assessment; identify lenders that merit special

attention in order to mitigate potential problems and SBA-guarantee losses; and monitor those lenders with higher risk profiles between on-site reviews.

The off-site monitoring approach is designed to have limited impact on lender operations. However, in cases where off-site monitoring identifies performance issues or concerns, OLO staff will follow-up directly with the lender to ascertain the reasons for and implications of changed performance. OLO may ask the lender to forward information and data to explain its SBA lending activity. Information requested may include a lender's SBA-guaranteed loan business profile; growth, expansion or contraction plans related to its SBA business; and/or loan liquidation activities. OLO may gather additional information through review of publicly-available annual reports and regulatory reports concerning the lender.

The off-site assessment also allows OLO to monitor lenders that are less active in terms of SBA-guaranteed loan volume. As a result of OLO's off-site assessment, OLO assigns a lender rating based on the level of risk OLO determines that a lender represents to SBA. The lender rating will determine the type of monitoring a lender will receive in the future. Off-site monitoring is an ongoing dynamic process.

On-Site Lender Reviews

OLO also conducts on-site reviews of SBA's more active lending partners. OLO uses a risk-based process to allocate its review resources to correspond with SBA guarantee exposure, resulting in more intensive and more frequent on-site review of those lenders with higher levels of risk and a less frequent and less intensive on-site review of lenders with relatively lower levels of risk.

These reviews are operational reviews and are not designed to duplicate the safety and soundness examinations that federally insured financial institutions are subject to by their primary regulators.

ON-SITE REVIEW PROCESS

Objectives of the On-Site Review

The on-site review process allows OLO to make an informed analysis of a lender's SBA-guaranteed loan program portfolio characteristics and lending operations, including loan originations, servicing, troubled asset management, and assessments of borrower eligibility. This information assists OLO in determining the level of program-related risk to SBA posed by that lender and its SBA-guaranteed loan portfolio and whether that level of risk is acceptable to SBA.

Reports prepared by OLO's on-site review team include a composite summary rating for the lender reviewed, supported by a detailed description and analysis of all material findings. As necessary, the report also will include recommendations for improvement and identify areas requiring the corrective action the lender must address.

Responsibility for Conducting On-Site Reviews

OLO's Kansas City Review Branch (KCRB) is responsible for managing and conducting on-site reviews and preparing review reports for SBA lenders, except for Small Business Lending Companies (SBLCs). SBLCs are subject to more intensive lender reviews conducted by the Farm Credit Administration on SBA's behalf.

KCRB maintains a staff of trained examiners on permanent duty. A review team led by an Examiner-In-Charge (EIC) will determine the scope of the review, identify special areas of interest, and select a sample of loan files to be reviewed. The EIC is an SBA employee and is guided in part by information obtained through off-site monitoring OLO previously has conducted for a lender and a comparative analysis to SBA portfolio performance.

KCRB also relies on outside resources to maximize effectiveness. Additional members of the review team are SBA employees and/or contractors, as needed, to accomplish the on-site review tasks. OLO and KCRB train all contract resources prior to their participation in on-site reviews.

Frequency of Review

Lenders subject to on-site reviews are initially identified through the quarterly loan and lender off-site assessment. On-site lender reviews are conducted on a 12 to 24 month cycle depending upon the level of risk a lender represents to SBA. The cycle may be accelerated based upon OLO's quarterly assessment of a lender and information that is obtained from other off-site monitoring activities.

Location of Review

Both the lender and the EIC will have input into determining the review site; however, the EIC will have final authority to decide on the location. The review will require access to the lender's senior management officials and a wide variety of data and information, including corporate governance and complete loan file documentation. Prior to commencement of the on-site review, the lender must deliver to the review site the material requested by OLO and the lender must put in place protocols that will permit its management to respond to OLO's inquiries in an effective and timely manner during the on-site review. This will result in the most effective use of OLO's lender review resources as well as the lender's resources.

Lender Notification

OLO will give lenders sufficient notification of the proposed review date to permit assembly of the necessary documentation and files. In setting the review date, the EIC will make an effort to select a date that is not unreasonably disruptive to the lender's operations.

Documentation and Files to be Reviewed

The EIC, on behalf of SBA, has regulatory authority to request and receive all documents and files deemed necessary to accomplish the objectives of the review. The EIC will provide the lender with a list of required documentation and loan files for on-site review approximately four weeks prior to the start of on-site activities. The EIC also may require the lender to provide additional documentation and files during the course of the review.

Exit Conference

Prior to the conclusion of the on-site review, the EIC will hold an exit conference with the lender. While the EIC will discuss with the lender the review team's observations and preliminary conclusions as the review progresses, the exit conference provides an opportunity for the EIC to summarize the observations and conclusions into one presentation. The exit conference also is designed to give the lender another opportunity to respond with additional information that could affect the review conclusions prior to SBA documenting the review results in a formal report.

Review Ratings

The primary outcome of an on-site review is to assess the overall quality of a lender's SBA lending activities. Based on this assessment, a lender rating is assigned. OLO will provide the lender with a Lender Review Report that discusses the review findings and recommendations and includes the rating assigned. OLO will distribute the report to the lenders as well as internally to those offices within SBA requiring such information. To the maximum extent allowed by law, SBA will maintain the strict confidentiality of all reports and associated ratings.

Report Distribution

A transmittal letter will accompany the hard copy of the report to the lender. The transmittal letter will clearly state the nature of any response and additional actions that OLO may require of the lender and the timeframe within which the lender must submit such response to SBA.

Action Plan (AP)

In certain cases, OLO may require a lender to submit an AP to address deficiencies identified during the course of the on-site review. OLO's transmittal letter will identify the requirements for an AP and the timeframe within which the lender must submit the AP to SBA. OLO will evaluate the adequacy of a lender's response and will notify the lender of the acceptability of the AP. OLO will monitor the lender's progress in meeting its AP, with the level of scrutiny appropriate for each deficiency cited in OLO's transmittal letter.

Cost of Reviews

SBA may charge lenders a fee to cover the cost of reviews, as appropriate.

SPECIAL PERFORMANCE ASSESSMENTS AND REVIEWS

In addition to regular on-site lender reviews, OLO also may conduct ad hoc or special performance assessments and reviews of a lender, as necessary. OLO will perform all such special assessments and reviews with full disclosure to and participation by the lender.

APPENDICES

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Appendix 1-A

Franchise Eligibility Checklist

Check Franchise Registry at www.franchiseregistry.com for applicant's Franchise.

When Franchise is on the Registry:

Ask Franchisor for Certificate

- ☐ Certificate of No Material Change received – Eligible: franchisor is not affiliated with the franchisee under the franchise agreement
- ☐ Certificate of Material Change received – New Eligibility determination required.
 - ☐ Send Certificate to FRANDATA and Senior Franchise Counsel. Wait for them to examine changes and determine affect on eligibility and let you know if the franchise is still eligible – **OR**
 - ☐ Send Certificate to FRANDATA and Senior Franchise Counsel. Then Determine eligibility as if the Franchise was Not listed on the Registry

When Franchise is Not in the Registry:

1. Ask Franchisor for Franchise Documents

- ☐ FTC Offering Circular (if they have one) or Current and Historical Financial and Litigation Information of the Franchise
- ☐ Franchise Agreement with Attachments & Amendments
- ☐ Referenced/Related Documents – Leases

2. Analyze Franchise Documents for Affiliation under 13 CFR 121.103(g):

Affiliation based on franchise and license agreements. The restraints imposed on a franchisee or licensee by its franchise or license agreement relating to standardized quality, advertising, accounting format and other similar provisions, generally will not be considered in determining whether the franchisor or licensor is affiliated with the franchisee or licensee provided the franchisee or licensee has the right to profit from its efforts and bears the risk of loss commensurate with ownership. Affiliation may arise, however, through other means, such as common ownership, common management or excessive restrictions upon the sale of the franchise interest.

3. Apply Franchise Eligibility Guidelines in SOP 70-50, Ch. 3., Para. 8 and Appendix 3e, and SOP 50-10, Para. A., Ch. 3, Sec. 3e:

Under the Franchise Agreement Franchisor must not control Franchisee, directly or through an agent, to such a degree that the Franchisee does not have the independent right to profit from its efforts and bear the risk of loss commensurate with ownership.

- ☐ Franchise Fee and other fees are not excessive
- ☐ Franchisee has control of money & accounts – deposits and withdrawals.
(Franchisor may prescribe accounting method and due dates for fee payment, but may not control accounts)
- ☐ Franchisee manages daily operations (except in case of illness or disability)
- ☐ Franchisee controls, hires and fires, employees (Franchisor can require employee training)
- ☐ Agreement specifies:
 - ☐ Events of default
 - ☐ What written Notice of default will be provided
 - ☐ Events that may lead to termination
 - ☐ Events that cause automatic termination
 - ☐ Time to cure provided for other defaults
- ☐ Franchisee has the right to transfer its interest in the franchised business:
 - ☐ Franchisor allows transfer to qualified transferee (Qualifications must be specified in Agreement or otherwise set forth in writing)
 - ☐ Franchisor prior written consent will not be unreasonably withheld or delayed
 - ☐ Franchisor does not control sale price or appraisal method
- ☐ Terms and conditions of leases and/or other franchise related documents do not lead to excessive Franchisor control
- ☐ EPC/OC Real Estate Loans: EPC directly leases 100% of space to the OC, not through an agent or subsidiary of the Franchisor
- ☐ Gas Station Loans: Effect of Petroleum Marketing Practices Act (PMPA)
- ☐ Determine if state law where the franchisee is located will affect any terms of Franchise Agreement and your eligibility determination.

4. Ask SBA whether there have been eligibility issues with this franchise

Send an e-mail to FRANCHISE@sba.gov or contact the Senior Franchise Counsel or local District Counsel to determine if this franchise has appeared on the Franchise Findings list, what problems there were, and whether franchisor was willing to negotiate a fix.

5. If eligible, get SBA Franchise Code Number, if ineligible try to negotiate a fix.

Existence of a SBA franchise code number does not mean the franchise is eligible. Comfort letters are not acceptable evidence of fixes. Franchisor must provide a written amendment if franchise agreement is changed or written agreement not to enforce a provision.

APPENDIX 4-A

QUICK REFERENCE GUIDE SOP 50 50 4 – SERVICING ACTIONS (Chapter/Paragraph)

The following is a selected list of servicing actions with the SOP reference. (For PLP, Express and LowDoc loans, see chapters 3, 4, and 5 for lender's delegated authority.)

<u>ACTION TYPE</u>	<u>SOP 50 50 4</u>	<u>ACTION TYPE</u>	<u>SOP 50 50 4</u>
Assumptions	Ch. 5/10	Reinstating SBA Guaranty	Ch. 10/3.a
Deferment	Ch. 5/8	Release of collateral/substitution*	Ch. 5/5.b
Exception to Policy	Ch. 2/4.i	Servicing (SBA to assume)	Ch. 9/17
Hazard Insurance	Ch. 5/18	Standby Agreement	Ch. 5/13
Interest Rate Adjustment	Ch. 5/16	Subordination	Ch. 4/17,5/8
Life Insurance	Ch. 5/19	Liquidation (transfer in)	Ch. 7/10
Maturity (extension of)	Ch. 5/5.b	Note Receivable	Ch. 7/5.g
UCC Continuation Filings	Ch. 4/7.b.1	Workouts	Ch. 7/5
Post Purchase Review	Ch. 9/10.c(1)	Purchase (Secondary)	Ch. 9/15
Transfer loans between District Offices	Ch. 3/1.d		
Transfer loans between Participant Lenders	Ch. 5/27		
Transfer loans to Fresno/Little Rock	Ch. 3/1.a		

Appendix 5-A

QUICK REFERENCE GUIDE SOP 50 51 2A – LIQUIDATION ACTIONS (and SOP 50 50 4A, SERVICING ACTIONS, where applicable)

(Chapter/Paragraph)

<u>ACTION TYPE</u>	<u>SOP 50 51 2</u>	<u>ACTION TYPE</u>	<u>SOP 50 51 2</u>
Abandonment	Ch. 11/34.a	Life Insurance	Ch. 22/2
Appraisals	Ch. 16/1.a	Liquidation Plan	Ch. 8/11.b
Assumption (SOP 50 50 4A)	Ch. 5/10	Maturity (Extension of) (SOP 50 50 4A)	Ch. 5/15.b
Auction	Ch. 15	Note (Sale of)	Ch. 4/14
Charge-Off	Ch. 18/2	Payment Application	Ch. 19/39.a and .b
Colpur (REO)	Ch. 11	Prior Lien Purchase/Payment	Ch. 21/5.f.(1) and (3)
Compromise	Ch. 17	Private Sale	Ch. 7/5.d
Compromise (without merit)	Ch. 17/7.c.3	Protective Bid	Ch. 7/10
Deed in Lieu of Foreclosure	Ch. 7/3.b	Protective Bid (tolerance range)	Ch. 7/14
Deferment	Ch. 5/4	Release of Collateral	Ch. 6/13
Environmentally Impaired Property	Ch. 6/15	Servicing (SBA to assume) (SOP 50 50 4A)	Ch. 9/17
Exception to Policy (SOP 50 50 4A)	Ch. 2/2.i	Taxes (Payment of R/E Taxes)	Ch. 20
Expenses (Payment of)	Ch. 19/8	Termination of Guaranty	Ch. 9/4.a
Forced Sale	Ch. 2/3.c	Title to Property	Ch. 11/5
Foreclosure (DOT)	Ch. 7/3.d	Transfer of loan to another lender (SOP 50 50 4A)	Ch. 5/27
Guarantors (Release of)	Ch. 12/12	Trustee Sale	Ch. 7/3.d
Insurance Coverage (Participant)	Ch. 22/1.a.3	UCC Release (Abandonment)	Ch. 6/23
Interest Rate Adjustment	Ch. 5/ 6 and 7	Workout	Ch. 5/1
Judgment	Ch. 12/16		
Late Fees (SOP 50 50 4B)	Ch. 3/9.a.3		
Legal Budget/Legal Fees	Ch. 8/22.b		
Legal Budget/Legal Fees (PLP)	Ch. 10/5.k		
Lender's Private UCC Sale	Ch. 8/19.a		
Liens (Senior Competing)	Ch. 21/1		
Liens (Competing Liens)	Ch. 8/10		

Appendix 5-B

LITIGATION PLAN

SBA LENDERS MUST SUBMIT A LITIGATION PLAN FOR PRIOR APPROVAL TO SBA COUNSEL FOR: (1) NON-ROUTINE (CONTESTED) LITIGATION INCLUDING ANY LITIGATION IN WHICH THE LENDER HAS ANOTHER OUTSTANDING LOAN TO THE BORROWER OR A GUARANTOR; AND (2) ROUTINE LITIGATION FOR WHICH OUTSIDE COUNSEL PROPOSES TO CHARGE FEES AND COSTS EXCEEDING \$5,000. LENDER MUST NOTIFY SBA COUNSEL IN WRITING WITHIN 15 DAYS OF THE DATE OF THE COMMENCEMENT OF ANY DEFENSIVE LITIGATION INVOLVING AN SBA GUARANTEED LOAN.

For a case requiring a Litigation Plan, you must provide the following:

Loan Name: _____

Loan Number: _____

1. Strategy, including what expert witnesses will be needed and their estimated cost and whether the case can be disposed of by motion or by trial;
2. Information regarding all non-SBA debts owed by the borrower, its owners and guarantors to the SBA participating lender, including the original amount of the obligation, current balance and current status;
3. Estimate of the recovery;
4. Risk of adverse precedent;
5. Actual or potential conflicts of interest;
6. Whether some form of Alternative Dispute Resolution (ADR) is advantageous, such as mediation, mini-trial or arbitration;

7. Settlement alternatives;
8. Estimated timetable; and
9. Any proposed pro-rata allocation of fees and recoveries, if lender has one or more loans to the borrower, its owner or guarantors that are not guaranteed by SBA.
10. Estimate of attorney's fees, including method of billing, and other litigative expenses.

AFTER APPROVAL OF THIS PLAN, YOU MUST:

1. **Submit legal bills to SBA counsel when received.**
2. **Submit substantive pleadings such as dispositive motions or other pleadings containing substantive legal arguments or statements of policy prior to filing; and**
3. **Submit an amended Litigation Plan as soon as modification of the plan is necessary or when the proposed legal fees and costs exceed the projections contained in the original litigation by 5 percent.**

LENDER

DATE

Appendix 6-A

QUICK REFERENCE GUIDE SOP 50 50 4, LOAN SERVICING, and SOP 50 51 2, LOAN LIQUIDATION, on GUARANTY PURCHASE

(Chapter/Paragraph)

<u>ACTION TYPE</u>	<u>SOP 50 50 4A</u>	<u>ACTION TYPE</u>	<u>SOP 50 51 2A</u>
Accrued interest (payment of)	Ch. 9/8	Amount of loss	Ch. 13/8
Acquisition of collateral (affect on purchase)	Ch. 9/12	Asset injection	Ch. 13/24.b
Determining earliest uncured default	Ch. 9/6	Borrower's injection	Ch. 13/24
Determining interest rate for purchase	Ch. 9/7	Burden of proof	Ch. 13/7
Information required of lender for purchase	Ch. 9/4	Cash injection	Ch. 13/24.a
Notice to lender of purchase	Ch.9/14	Change of ownership	Ch. 13/21.b & 23
Receipt of funds from SBA	Ch. 9/11	Collateral available at liquidation	Ch. 13/22.b
Regulation	Ch. 9/2	Collateral lien position	Ch. 13/26
Review of loan documentation	Ch. 9/10	Collateral lists at time loan is made	Ch. 13/27
Purchase from secondary market	Ch. 9/15	Denial of liability (SBA official w/authority)	Ch. 13/1
Purchase log	Ch. 9/19	Denial of liability (evaluation of)	Ch. 13/3
SBA's purchase of unguaranteed portion	Ch. 9/18	Determining amount of loss attributable to lender	Ch. 13/23
SBA's unilateral purchase privilege	Ch. 9/13	Early default/early loan problems	Ch. 13/14, 22.c.(i), & 21.a
Verification of lender's transcript	Ch. 9/9	Establishing loss if collateral is missing at liquidation	Ch. 13/22.c
When SBA purchases	Ch. 9/3	Expiration of guaranty after maturity	Ch. 13/25
When lender must submit complete purchase	Ch. 9/5	File documentation	Ch. 13/12
		IRS delay	Ch. 13/21
		IRS tax verification	Ch. 13/21
		Length of time in business	Ch. 13/24.c
		LowDoc eligibility	Ch. 13/16
		Program integrity	Ch. 13/9

Appendix 6-B

GUARANTY PURCHASE CHECKLIST

SBA Loan Number: _____ **SBA Loan Name:** _____

Instructions: Items pre-checked are mandatory for all purchases. Additional checked items are necessary to determine liability of SBA to honor its guaranty for this loan. If a required item is not available, Lender must provide a written explanation. Lender must **not** deliver or assign any original collateral documents to SBA unless directed to do so by SBA.

Note: For purchases under the Streamlined Guaranty Purchase Process (SBA share \$10,000 or less) go to next page.

BANK	REQ'd of REC'd	SBA USE ONLY NEED	
<u>ADMINISTRATIVE DOCUMENTS</u>			
1	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Written demand that SBA honor its guaranty
2	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Wire transfer instructions
3	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Certified Transcript of Account signed by lender; transcript must include payment receipt dates, interest rates in effect, amounts applied to principal and/or interest; transcript must show all transactions on borrower's account including liquidation receipts and expenses, along with date of default, interest rate at default, date to which interest has been paid and next installment due date
<u>SBA POLICY / SOP REQUIREMENTS</u>			
4	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Executed Loan Authorization and any amendments
5	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Settlement Sheets (SBA Form 1050). Attach evidence showing proceeds were used according to the Authorization and instructions on SBA Form 1050; include copies of cleared joint payee checks, bills of sale and paid invoices, as applicable
6	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Risk Management Database information
7	<input type="checkbox"/>	<input type="checkbox"/>	Evidence of borrower Injection (such as copies of cleared checks, bank statements, escrow closing statements, paid invoices); required if injection is a condition of the loan authorization
8	<input type="checkbox"/>	<input type="checkbox"/>	IRS Income Tax Verification for years _____
9	<input type="checkbox"/>	<input type="checkbox"/>	Lender's credit memorandum and supporting documentation (PLP/SBAExpress early default loans)
10	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Loan eligibility determination (PLP loans only)
11	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Loan eligibility checklist and supporting documentation (LowDoc loans only)
12	<input type="checkbox"/>	<input type="checkbox"/>	Liquidation Plan
13	<input type="checkbox"/>	<input type="checkbox"/>	Site Visit Reports
14	<input type="checkbox"/>	<input type="checkbox"/>	Liquidation Wrap-up Report with supporting documentation
<u>DEBT INSTRUMENTS</u>			
15	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Note (SBA Form 147) with any Modifications/Amendments
16	<input checked="" type="checkbox"/>	<input type="checkbox"/>	Guaranties (SBA Form 148)
17	<input type="checkbox"/>	<input type="checkbox"/>	Evidence of guarantor consent for any material changes to the loan terms
<u>REAL ESTATE COLLATERAL</u>			
18	<input type="checkbox"/>	<input type="checkbox"/>	Recorded Deeds of Trust / Mortgages covering _____
19	<input type="checkbox"/>	<input type="checkbox"/>	Transfer and Assignment of Deeds of Trust / Mortgages to SBA (only if SBA services)
20	<input type="checkbox"/>	<input type="checkbox"/>	Title Insurance Policies and/or Certificates
<u>PERSONAL PROPERTY COLLATERAL</u>			
21	<input type="checkbox"/>	<input type="checkbox"/>	Security Agreements
22	<input type="checkbox"/>	<input type="checkbox"/>	UCC Financing Statements filed with Secretary of State and/or County
23	<input type="checkbox"/>	<input type="checkbox"/>	UCC Continuation Statements and Amendments

24	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	UCC Financing Statements with assignments to SBA
25	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Post Default UCC Lien Searches, including copies of all filings
26	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Landlord's Subordination / Waiver
27	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Certificate of Ownership and/or Certificate of Title on Vehicles / M&E / Manufactured Homes
28	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Transfer and assignments of Vehicle / M&E / Manufactured Home titles to SBA (only if SBA services)
 INSURANCE REQUIREMENTS				
29	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Life Insurance Policies (summary pages only)
30	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Collateral Assignment of Life Insurance Policy (acknowledged by Insurance Company)
31	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Transfer and Assignment to SBA of Collateral Assignment of Life Insurance Policy (only if SBA services)
32	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Hazard Insurance Policies (page showing insured, amount & mortgagee will suffice)
33	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Evidence of Standard Flood Insurance Policy or determination that property is not located in a special flood hazard area
 OTHER MISCELLANEOUS DOCUMENTS				
34	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Reconciliation of original collateral, with a unit value of \$500 or more (include description and serial numbers) to current inventoried collateral
35	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Demand Letters
36	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Copies of all legal pleadings, including bankruptcy filings
37	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Itemized legal invoices, including hours per task and charge per hour
38	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Itemized expenditures (these expenditures should match the Transcript of Account)
39	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Reports for sale of collateral
40	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Appraisals received at loan origination and liquidation (summary pages only)
41	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Lease Agreement (pages showing terms, lessee & signatures)
42	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Environmental Questionnaires on _____
43	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Phase I and/or Phase II Environmental Report (Summary & Recommendation pages only)
44	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	SBA Form 912, Statement of Personal History, for each principal (required for PLP/SBAExpress early default loans)
45	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Other: _____
46	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	Other: _____

IMPORTANT: When instructed to transfer servicing to SBA and original documents are required, the Note (and any Modifications/Amendments), Guaranties, and Security Agreements must have the following typed on them and be signed and dated by the Lender: **"Transferred and assigned to the U.S. Small Business Administration, an Agency of the U.S. Government, without recourse."**

CHECKLIST FOR STREAMLINED SMALL LOAN BALANCE PURCHASES (SBA share \$10,000 or less)

BANK	REQ'd of		SBA USE ONLY NEED	
	REC'd			
1 <input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		Written demand that SBA honor its guarantee including date of default, interest-paid-to date, interest rate at time of default, and the next installment due date.
2 <input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		Wire transfer instructions
3 <input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		Certified Transcript of Account signed by lender <i>(must include the payment receipt dates, the interest rates in effect, and the amounts applied to principal and/or interest. The transcript must show all transactions on the borrower's account including liquidation proceeds and expenses)</i>
4 <input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		Lender's documentation of eligibility (PLP and Lowdoc loans only)
5 <input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>		Copies of Note, executed Loan Authorization and any guaranties

6 ☒ ☐ ☐ Risk Management Database information

7 ☒ ☐ ☐ Lender certification that loan proceeds were disbursed in accordance with the loan authorization

IF LIQUIDATION IS COMPLETE:

7 ☒ ☐ ☐ Lender certification that liquidation is complete and that all avenues of collection have been completed

8 ☒ ☐ ☐ Final wrap-up report with information required by SOP 50 51 2